

# THE ADMINISTRATIVE STATE: AN EXAMINATION OF FEDERAL RULEMAKING

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## HEARING

BEFORE THE

COMMITTEE ON  
HOMELAND SECURITY AND  
GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE  
ONE HUNDRED FOURTEENTH CONGRESS

SECOND SESSION

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## **THE ADMINISTRATIVE STATE: AN EXAMINATION OF FEDERAL RULEMAKING**

**WEDNESDAY, APRIL 20, 2016**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Committee met, pursuant to notice, at 10:11 a.m., in room 342, Dirksen Senate Office Building, Hon. Ron Johnson, Chairman of the Committee, presiding.

Present: Senators Johnson, Portman, Ayotte, Ernst, McCaskill, Tester, Baldwin, Heitkamp, and Peters.

### **OPENING STATEMENT OF CHAIRMAN JOHNSON**

Chairman JOHNSON. Good morning. This hearing is called to order.

I have a little script here, which is unusual for me, so let me just read it. I ask unanimous consent that my full opening statement be entered into the record.<sup>1</sup>

Senator McCASKILL. Without objection.

Chairman JOHNSON. Without objection, so ordered.

Senator Carper had a death in his family, his aunt, who he was very close to, so he will not be here today. We obviously send our sincere condolences to Senator Carper and his family, and I ask unanimous consent that his opening statement be entered into the record.<sup>2</sup>

Senator McCASKILL. Without objection.

Chairman JOHNSON. Without objection, so ordered.

I also ask unanimous consent that the following documents be entered into the record: The Majority Staff report<sup>3</sup> titled “The Labor Department’s Fiduciary Rule: How a Flawed Process Could Hurt Retirement Savers;” the Minority Staff memo<sup>4</sup> on the Labor Department’s financial fiduciary rule; the Majority Staff report titled, “Regulating the Internet: How the White House Bowled Over the Federal Communications Commission (FCC) Independence;”<sup>5</sup> and a January 14, 1991, Office of Legal Counsel memorandum ti-

<sup>1</sup> The prepared statement of Senator Johnson appears in the Appendix on page 41.

<sup>2</sup> The prepared statement of Senator Carper appears in the Appendix on page 43.

<sup>3</sup> The Majority report titled The Labor Department’s Fiduciary Rule appears in the Appendix on page 190.

<sup>4</sup> The Minority Memorandum on the Labor Department’s proposed conflict of interest rule appears in the Appendix on page 260.

<sup>5</sup> The Majority report titled Regulating the Internet: How the White House Bowled Over FCC Independence appears in the Appendix on page 230.

tled, “Ex Parte Communications During FCC Rulemaking.”<sup>1</sup> Without objection, so ordered.

I want to thank all of the witnesses for testifying here today and for taking the time and writing up what I think is some very thoughtful testimony. You did a good job, pretty thick testimony which will all be entered into the record. When you do speak, try to keep it down to about 6 minutes and then we will do rounds of questions.

From my standpoint, this is just an incredibly important hearing. I have said repeatedly—well, first of all, this Committee actually has a mission statement. I come from a business background, so it is something Senator Carper and I developed. It is pretty simple, to enhance the economic and national security of America. Those are inextricably linked.

How do you get a strong economy? From my standpoint, we are the world’s largest market, which is an enormous advantage in the global competition. We do have cheap and abundant energy. We should keep it that way while we protect our environment.

Our weaknesses are we have an onerous regulatory environment, and we will probably have some differences of opinion on that, but, numerous studies talk about how the cost of Federal regulations are somewhere between \$1.8 and \$2 trillion. To put that number in perspective, only 9 or 10 economies in the world exceed \$2 trillion. That is an enormous self-inflicted wound and burden.

And, yes, I realize we need some regulations, and they protect workers and they protect our environment. That is a good thing. But, there is a point of over-regulation. We will talk a little bit about that.

We hear about income inequality, which is a real problem. We hear about stagnant wages. Talking to one chief executive officer (CEO) of a paper manufacturing company in Wisconsin, he did a little cost study on just four regulations issued by this administration, just four, and, of course, we have hundreds of major regulations costing over \$100 million. But, just four regulations, the cost to this paper company was the equivalent of \$12,000 per employee per year. So, if you are wondering why wages have stagnated, look no further than the regulatory burden placed on the private sector by big government here in Washington, D.C. It is an enormous burden and we have to recognize that fact.

The last point I will make, the Chancellor of the University of Wisconsin-Madison, Rebecca Blank, has come into my office the last 2 years, both times asking for relief from regulations. This last year when she came in, she had a research study. It was actually called the 2012 Faculty Workload Survey, done by the Federal Demonstration Partnership Research Report from April 2014, and basically, what that research showed is that 42 percent of researchers’ times in the research university are spent complying with Federal regulations—42 percent. Now, those research dollars, that grant money is spent to go into basic science, advancing human knowledge, curing diseases. If 42 percent of their time is spent just

<sup>1</sup>The Minority submission of the OLC Opinion titled Ex Parte Communication During FCC Rulemaking appears in the Appendix on page 268.

complying with Federal regulations, think of the opportunity cost of that.

So, again, the regulatory burden is a serious problem. We are going to be talking about just three rules where I think there are some real questions as to whether this administration issued those properly, not violated the Administrative Procedure Act. We are going to be talking about the Fiduciary Rule, the Federal Communications Commission Title II Internet regulation, and the Waters of the United States (WOTUS). I mean, these are three significant rules that are going to have a significant impact on our economy. The number one solution for debt and deficit or so many problems is economic growth and these regulations are stifling it.

So, with that, it is the tradition of this Committee to swear in witnesses, so if you will all rise and raise your right hand.

Do you swear the testimony you will give before this Committee will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. MAY. I do.

Mr. KOVACS. I do.

Mr. TURLEY. I do.

Mr. CAMPBELL. I do.

Mr. WEISSMAN. I do.

Chairman JOHNSON. Please be seated.

Our first witness is Professor Jonathan Turley. Professor Turley is the Shapiro Professor of Public Interest Law at the George Washington University Law School. Professor Turley.

**TESTIMONY OF JONATHAN TURLEY,<sup>1</sup> SHAPIRO PROFESSOR OF PUBLIC INTEREST LAW, GEORGE WASHINGTON UNIVERSITY LAW SCHOOL**

Mr. TURLEY. Thank you so much, Chairman Johnson and Members of the Committee. It is a great honor to appear before you today to talk about the rise of the administrative State within the American constitutional system.

I come to this with more of a constitutional perspective than an administrative law perspective. I have long been critical of the rise of what is often called the fourth branch in our system. And, while academics have good faith disagreements, I tend to view the rise of the administrative State as neither benign nor inevitable. I think it is a problem that we often treat this concept of administrative State as a *fait accompli*, like a reality like the weather, in our constitutional system. And, those of us who criticize it often appear quixotic, tilting at the windmills of Federal agencies.

It is not a criticism of Federal agencies to question the degree of discretion and delegation that they currently enjoy, no more than it is to say that we need banks as an answer to calls for banking reform. The Federal agency is a reality of our system. It is part of modern government. But, the degree to which we have delegated authority, legislative authority, and discretion to the Federal agencies, in my view, is dangerous.

Indeed, I doubt the Framers would recognize the system we have today. Well, they would recognize it in one sense. It is, in many re-

<sup>1</sup> The prepared statement of Mr. Turley appears in the Appendix on page 47.

spects, the system they sought to avoid. The Framers were focused on the danger of concentrated power and the need for participatory representative politics. Neither of that is present in the current system.

Rulemaking is a virtual euphemism for agency legislation, and the two examples of that that I will discuss today, hopefully in more detail, include the *United States v. Texas* controversy over Deferred Action for Parents of Americans (DAPA), which showed how truly Section 553 of the Administrative Procedure Act (APA) has become without substance. The administration effectively ordered unilaterally changes that were denied by Congress. They did that not only through executive power, but, they even refused to do the notice and comment requirements under the APA. I have been a critic of the APA as a paper tiger, but in this case, it was not even that.

The net neutrality controversy is another good example. I do not necessarily want to weigh in on the merits. There are smarter people that know a lot more about net neutrality and immigration than I do. I am much more concerned with the process, that is, what we have seen is the transfer of legislative powers to an opaque system where citizens have very little role or very little knowledge. The fact that you can have a visit with Chairman Tom Wheeler and have the change of a position of the FCC, it really speaks volumes to the problems that we are having now in terms of the shift from a representative democratic system to a more bureaucratic system.

My fear is that while we can reverse this trend, we are fast approaching a certain constitutional failsafe line where the administrative state will become a fixed and unassailable reality of American government. I happen to agree with many things that President Obama has tried to achieve. I just do not agree with the means by which he is trying to achieve them.

I am, in many ways, a stereotypical Madisonian scholar. I believe that the Legislative Branch is the thumping heart of our constitutional system and it is increasingly becoming irrelevant. I think that members are allowing the power of this institution to slip away into the midst of an administrative state.

My testimony includes various things that can be done, but it cannot be done on the cheap. Congress has to join in a bipartisan way to fight for its authority the way the Framers thought that you would. This includes dealing with the discretion that is afforded under Chevron, the creation of non-delegation provisions to ensure that this body remains relevant, greater oversight with teeth in terms of agencies, the creation of an office that will focus more substantially on rulemaking, new APA procedures, new consent laws that have guillotine switches so that major regulations will come before this body, and finally, empowering citizens to help Congress monitor what has become a fourth branch in our system. All of these things can be done.

I do not wish to sound particularly dire, but I believe this is a dire situation. I believe that what we are seeing is a different type of government. Now, it may be a better system according to some academics, but it is a system that the American people were never allowed to voice their view of. It is a substantial change in what



we call the American governmental system. It is less representative. It is less transparent. And, I believe that, in the end, it is destabilizing.

As my testimony states, the Legislative Branch plays a critical role in transforming factional disputes. On this table, there are experts who I look forward to hearing from who are going to raise very important arguments on both sides of these divisive questions, but the Nation is divided. And, when we are divided, this is the body that was designed to transform those factional disputes into majoritarian compromises. If you remove these questions from Congress, you add the very instability that the Framers wanted to avoid and you are shifting it far away from the center of power.

So, the center of gravity in our system has changed, but we can regain it, and I believe that should be a matter that all members and all citizens should join together to see.

Thank you very much.

Chairman JOHNSON. Thank you, Professor Turley.

Our next witness is Randolph May. Mr. May is the founder and President of the Free State Foundation (FSF). Mr. May previously served as Assistant General Counsel and Associate General Counsel at the Federal Communications Commission from 1978 to 1981. Mr. May.

**TESTIMONY OF RANDOLPH J. MAY,<sup>1</sup> PRESIDENT, THE FREE  
STATE FOUNDATION**

Mr. MAY. Mr. Chairman and Members of the Committee, thank you for inviting me to testify today. I am President of the Free State Foundation, a think tank that focuses its research primarily in the communications law and policy and administrative law areas. I have been involved for almost 40 years in communications law and policy in various capacities, including having served as Associate General Counsel at the FCC. My longstanding expertise at the intersection of communications law and policy and administrative law is outlined in my written testimony.

The Committee's identification of the FCC's net neutrality rule as deserving of examination is wise. This rulemaking is instructive regarding the ways in which a faulty rulemaking process enables the growth of the administrative state and adversely impacts the economy, and in the case of the net neutrality rulemaking, compromises accepted rule of law norms.

I want to highlight briefly in my oral testimony four areas in which the FCC's net neutrality rulemaking is problematic.

First, the rulemaking truly represents a case of the proverbial solution in search of a problem, or, as FCC Commissioner Ajit Pai put it recently, the rule, "was a 313-page solution that would not work to a problem that did not exist." Put bluntly, in this case, there was no meaningful evidence of an existing market failure or consumer harm that required the Commission to adopt rules applying heavy-handed Ma Bell-era public utility-like regulation to today's Internet service providers (ISPs).

The dynamic, competitive marketplace in which Internet service providers operate today is far removed from the staid monopolistic

<sup>1</sup> The prepared statement of Mr. May appears in the Appendix on page 67.

markets for which public utility regulation was devised, when, for example, it was applied to the railroads in 1887 and then to telephone and telegraph companies in 1934, when the Communications Act was adopted. There was no reason for the FCC to ignore Congress's direction in the 1996 Telecom Act that the Internet should remain, "unfettered or by Federal or State regulation."

Second, as a result of the direct and indirect cost imposed on Internet service providers, the rules adoption most likely will have an adverse impact by chilling investment and innovation. Indeed, there is some persuasive evidence that it is already doing so. Of course, diminished investment in innovation translate into diminished jobs and consumer welfare.

Third, the manner of President Obama's direct involvement in the FCC's net neutrality rulemaking in the aftermath of his involvement that resulted initially in confusion at the FCC, and then shortly afterward in an abrupt change in course that conformed to President Obama's specific ask, raise questions about the FCC's supposed independence. The manner in which the rulemaking was conducted serves to undermine the notion of the FCC's independence in an agency whose decisions are primarily based on its specialized expertise rather than on political considerations. And this, in turn, jeopardizes the public's confidence in the soundness of the Commission's decisions and the agency's institutional integrity.

Of concern, just last week, the White House released a high-profile statement urging the FCC to adopt a specific course of action in the agency's controversial and very problematic video navigation rulemaking. Repeated high-profile Presidential interventions like this further undermine the notion that the FCC acts independently and free from Executive Branch control.

Finally, aside from issues relating to President Obama's involvement, there are aspects of the net neutrality rule, specifically including adoption of the vague general conduct rule, which itself the FCC admitted is a, quote, "catch-all provision," along with a catch-22 enforcement regime that the rule established, that call into question compliance with accepted rule of law and due process norms. These norms require that law be predictable and knowable in advance of the imposition of sanctions, which in the case of the net neutrality rule certainly is not the case. Failing to adhere to these norms also threatens to undermine the public's confidence in the agency's institutional integrity.

Again, thank you for giving me the opportunity to testify today and I look forward to answering your questions.

Chairman JOHNSON. Thank you, Mr. May.

Our next witness is the Honorable Bradford Campbell. Mr. Campbell is the former Assistant Secretary of Labor for Employee Benefits. Mr. Campbell currently practices employee benefits law with the law firm Drinker Biddle and Reath. Mr. Campbell.

**TESTIMONY OF THE HONORABLE BRADFORD P. CAMPBELL,<sup>1</sup>  
COUNSEL, DRINKER BIDDLE AND REATH, LLP, AND FORMER  
ASSISTANT SECRETARY FOR EMPLOYEE BENEFITS AT THE  
U.S. DEPARTMENT OF LABOR**

Mr. CAMPBELL. Well, thank you, Mr. Chairman and the Members of the Committee, the other Senators, for the opportunity to testify today about the need to reform the Federal regulatory process.

Before I begin, though, I want to advise you that the views I express today are my own, not those of any client or my firm or my colleagues.

The sheer scope of Federal regulation is remarkable. What we eat, what we wear, what we drive, how we work, how we save, even the air we breathe, nearly every activity of our lives is now at least partially subject to Federal regulations. While there is, of course, a necessary role for Federal regulation in interstate commerce, I think it is fair to say that the current regulatory environment and the practices of some Federal regulators are in significant need of review and reform.

The regulatory authority that Congress delegates to Federal agencies was never intended to allow those agencies to become their own quasi-legislative bodies, making new laws and policies as they see fit. Instead, that authority was intended to facilitate the practical implementation of laws passed by Congress so that agencies could promulgate rules consistent with the intent and direction of Congress, and finalized only after a thorough and fair consideration of the economic impact, costs, and the alternatives available. Unfortunately, the reality of the Federal regulatory process all too often does not actually match this intent.

Now, I am going to focus today on a particular example of regulatory overreach, the recently promulgated final regulation by the U.S. Department of Labor (DOL) redefining fiduciary investment advice. This incredibly broad and far-reaching rule makes the Department of Labor a primary regulator of the conduct and compensation of financial advisors to more than \$14 trillion—that is trillion with a “t”—in Individual Retirement Accounts (IRA) and retirement plan assets, and it effectively allows the Department of Labor standards to trump the traditional role of other regulators, like the Securities and Exchange Commission (SEC).

I am very familiar with this regulation and with this agency’s authority, because as the Chairman noted, I used to run this agency in the prior administration.

This fiduciary regulation highlights what I see as two primary issues facing the Committee when considering reform. First, it was legislation by rulemaking, in which an agency fundamentally changes the law, and in this case counter to Congressional intent, taking over Congress’s role.

And, second, it was an exercise of flawed regulatory process in which predetermined policy decisions drove the outcome, not real consideration of economic inputs or regulatory alternatives.

Now, this real clearly is legislation by regulation. It was created out of whole cloth by the agency. The underlying law that it is interpreting, this potion has not changed since 1974, when it was

<sup>1</sup> The prepared statement of Mr. Campbell appears in the Appendix on page 88.

passed. And, in fact, the changes the rule ultimately makes, at least many of them, are contrary to the intent of Congress when it passed those laws.

Congress created the Employee Retirement Income Security Act (ERISA) plans and IRAs at the same time, and it affirmatively chose not to apply the new fiduciary standard and new legal remedies that it created for ERISA plans to IRAs. Instead, Congress chose for IRAs to be protected through extensive Federal and State regulation of financial services with their applicable standards of care and legal remedies.

Remarkably enough, these intentional Congressional decisions were cited as flaws by the Labor Department that it must correct to preserve Congressional intent. The Department, which, acting based on a Carter Administration reorganization of authority divided between the Labor Department and the Treasury Department, applied its new and very broad definition of fiduciary to the prohibited transaction rules in the tax code, and these rules apply to IRAs.

The effect of this was to make advisor compensation that is legal under securities laws illegal under the tax code, and the Department of Labor then created an exemption, called the Best Interest Contact Exemption, which permitted some of that securities law compensation to remain legal, but only if the financial institution and the advisor agree to an ERISA-like fiduciary standard of care and to being sued in State court in class action litigation.

So, in short, the Department in this regulation is forcing IRA advisors to accept a fiduciary standard and legal remedies that Congress affirmatively chose not to require, all in the name of Congressional intent.

Now, whether you agree with the Department of Labor that IRAs should be treated more like ERISA plans or not is irrelevant for the purposes of this hearing. I think the issue should be that only Congress should overturn the prior judgments of Congress, not a Federal agency through a convoluted misapplication of its regulatory authority.

And, further, as this Committee's report amply demonstrates, the Majority report the Chairman previously entered into the record, the Department did not follow the requirements of the Executive Orders (EO) and the Office of Management and Budget (OMB) guidance governing the proper development of Federal regulations, the cost estimates and considerations of regulatory alternatives. E-mail exchanges in that report between the SEC staff and Labor officials revealed that the Department of Labor at the proposal stage refused to fully consider some of the alternative regulations on the grounds that doing so would be too time consuming. The staff at the Treasury Department raised concerns about whether the Department's use of this authority was, in fact, consistent with Congressional direction in the rule.

And the final rule continues to have unrealistic cost estimates, such as assuming that legal counsel that comply with the new rule will cost, on average, \$134 an hour, which I think if you have gone out and priced legal counsel, particularly in a specialty area like ERISA, is a little bit underpriced.

They further estimated that it would take 10 minutes of one lawyer's time to make certain disclosure changes, on which liability under a class action in State court might hinge. I assure you, it is going to cost more than \$22.33 to analyze that particular provision for anyone complying with this rule.

To conclude, as I described in more detail in my written testimony, I think the Committee should consider consolidating these fragmented requirements, some of which are in Executive Orders, some of which are overseen by OMB, some of which are in the law, to engage in a comprehensive legislative process that would make valid economic analysis and other essential elements of this process enforceable.

Thank you very much for the opportunity and I look forward to any questions.

Chairman JOHNSON. Thank you, Mr. Campbell.

Our next witness is William Kovacs. Mr. Kovacs is the Senior Vice President for the Environment, Technology, and Regulatory Affairs at the U.S. Chamber of Commerce. Mr. Kovacs.

**TESTIMONY OF WILLIAM L. KOVACS,<sup>1</sup> SENIOR VICE PRESIDENT, ENVIRONMENT, TECHNOLOGY, AND REGULATORY AFFAIRS, U.S. CHAMBER OF COMMERCE**

Mr. KOVACS. Thank you, Mr. Chairman, for inviting me to testify on *The Administrative State: An Examination of Federal Rulemaking*.

Before beginning my testimony, I would like to thank the Committee for its bipartisan passage of the Federal permit streamlining legislation last year and for Chairman Johnson, Senators Portman and McCaskill, for their leadership on the effort.

On the Waters of the United States, the Chamber greatly appreciates the efforts of Senator Heitkamp, a consistent leader on the effort, she has put forth in S. 1140 a very practical and workable solution to the Waters issue.

Now, turning to examining Federal rulemaking, how Federal regulations are developed by agencies should be a bipartisan priority for Congress so as to ensure that the legislative powers that Congress delegates to the agencies are used to achieve Congressional intent.

Controlling Federal agencies has been a challenge to Congress since the first agency was created in 1887. To circumscribe the legislative powers of agencies, Congress enacted the Administrative Procedures Act in 1946, and it has not been amended since then, to ensure fairness to affected parties by allowing them to test the soundness of an agency's proposal through exposure to public comment and to develop evidence in the record to support their views so that you can have clear judicial review.

Unfortunately, due to the broad laws passed by Congress, the APA's informal rulemaking process has morphed into a process that allows agencies to issue very expansive regulations that are well beyond anything Congress intended. And, with the courts granting considerable deference to the agency decisions, agencies

<sup>1</sup>The prepared statement of Mr. Kovacs appears in the Appendix on page 110.

avoid the stringent judicial review that is required by an independent agency and the Constitution.

The consequence of this is regulations like WOTUS that are far broader in scope than Congress ever intended. Yet, these regulations are imposed by agencies with little effort. Legislating is hard work, but agencies can legislate with little work.

In the WOTUS rule, the Environmental Protection Agency (EPA), under the pretext of clarifying a definition, added several new definitions, unintelligible definitions, to existing definitions, thereby producing a rule so confusing and all encompassing that the agencies could bring their jurisdiction to nearly every water feature and associated land under its jurisdiction. In essence, EPA turned itself into a national zoning board.

The WOTUS rule has resulted in such uncertainty that 30 States and many stakeholders have filed lawsuits in 12 Federal District Courts and eight Federal Circuit Courts.

EPA produced this unworkable rule by simply ignoring the procedures Congress had put in place for years and decades. They failed to evaluate the impacts under the Unfunded Mandates Reform Act (UMRA). They failed to look at the Information Quality Act (IQA). They ignored the Regulatory Flexibility Act (RFA). And, they failed to examine and do the analysis on job impacts for almost 40 years.

Had EPA followed Congress' direction, it would have learned that the States, not EPA, implement 96 percent of EPA's delegated programs, and that by placing more and more of these massive regulations on the States without any new funding, it is straining the implementation, and that is really crucial, because if they are implementing 96 percent and in a 6-month period of time EPA put on ozone, Waters of the U.S., and clean power, that is amazing for a group of individuals who are not getting any more money than they got literally 20 years ago.

EPA would have discovered, also, in the Waters of the United States, that counties—this was a point totally ignored by the agency, because they said we do not have to do unfunded mandate reviews—that counties that build and maintain almost half the roads in the United States, and under WOTUS, all of these counties, just to move dirt along the thousands of miles of roadside ditches that WOTUS considers tributaries, they are going to need a permit. And a dredge and fill permit costs about \$150,000 per permit.

So, moreover, the Government Accountability Office (GAO) then found that the millions of EPA's alleged supporters were the creation of social media, which was a violation of the anti-lobbying statute.

Here is the challenge for Congress. You cannot look at every rule. You have to preserve the efficiency of the informal process for the vast bulk of the 4,000 rules a year. But, for those rules that are extraordinarily complex and costly, and there are not a lot of them, the agencies must be required to do the extra homework to consult with the various parties. And, again, I do not want to keep on referring to S. 1140, but it is one of the requirements and it is very clear, and that is so important to getting the rule right.

The agencies, when they are doing this, they need to ensure that they are going to do the extra work, but one of the bills that is before this Committee, S. 2006, the Regulatory Accountability Act

(RAA) introduced by Senator Portman and referred to this Committee, really strikes that balance. The House has passed it four times and it is really time for the Senate to begin taking up this, because what it does is it distinguishes between the 3,700 regulations that basically keep society running and the five to 50 regulations that really cause problems, and it is so important.

And, what it does is it establishes a clear process for the agencies to follow and clear procedures that the courts can review. It requires greater transparency, more homework by the agencies on complex rules, discussions with impacted parties, and understanding of the impacts of unfunded mandates, and a mechanism that allows the public to question the agencies to ensure that Congressional intent is achieved. I recommend you looking at this bill in any way.

Thank you for allowing me to testify today and I would be glad to answer any questions.

Chairman JOHNSON. Thank you, Mr. Kovacs.

Our final witness is Robert Weissman. You have a pretty short bio here. You are the President of Public Citizen. Mr. Weissman.

**TESTIMONY OF ROBERT WEISSMAN,<sup>1</sup> PRESIDENT, PUBLIC CITIZEN**

Mr. WEISSMAN. Thank you very much, Chairman Johnson and Members of the Committee. My written testimony goes into some detail about the three case studies of this hearing. My oral remarks will be focused more generally on the regulatory process itself.

I wanted to make three points. The first is that although people focus on process all of the time, really underlying the thinking about process is some views about the benefits and costs of regulations themselves. And, so, I think we really should have as a starting point a recognition that regulation has made our country stronger, safer, more secure, cleaner, and healthier. It has made our economy stronger. It has reduced the risk of financial risk when regulations were properly maintained. It made our food safer, our cars safer. It made it easier to breathe, improved children's brain development, empowered disabled persons, guaranteed a minimum wage, and far more.

When there are serious efforts to try to weigh the costs and benefit of regulation, it is a problematic exercise, but the best effort by far is from OMB, which uses very conservative accounting methods for benefits. It finds, at a minimum, benefits outweigh costs by 2-to-1, and maybe by as much as 15-to-1, consistently across time, across administrations.

Chairman Johnson, you mentioned the \$2 trillion figure for cost. I think if you examine the studies that make those claims in more detail, you will find that they are not credible studies. I am happy to discuss that further.

Costs, it turns out, are regularly and routinely overstated by industry for understandable reasons. But, if we look back historically at most of the most severe claims about costs of impending regulation, it turns out retrospectively that the apocalyptic claims did not come true, for the environmental area, worker health and safety,

<sup>1</sup> The prepared statement of Mr. Weissman appears in the Appendix on page 141.

a vast array of consumer protection. Many of these are detailed in my written testimony.

Additionally, there is no good evidence that regulation contributes to job loss. Before ending its survey for budgetary reasons, the Department of Labor collected information on why employers laid people off, and they rarely referenced regulation as the reason.

Finally, in terms of thinking about benefits and costs of regulation, we should recognize the cost of regulatory failure. And if we are thinking about the economy at all, the most significant fact of our recent time, or even in the last 70 years in the economy, is the collapse in 2008. There is no way to understand what happened, whatever your accounting of it is, there is no way to understand that as anything but the result of a regulatory failure. The cost to the economy was on the order of \$20 trillion, far exceeding any plausible cost of regulation.

My second point, although I think it is important to understand the benefits of regulation, and the benefit as opposed to cost, there certainly are severe problems with the regulatory process. I think the number one for any of us involved in the rulemaking process is extended and unreasonable delay. Those delays have very real costs both in accruing the benefits of regulation and in denying businesses the certainty they need to make appropriate investment decisions.

A bunch of case studies in my written testimony. Just to quickly reference two, Congress in 2008 passed a law requiring auto makers to install backup cameras or equivalent in their automobiles. You all set a statutory deadline of 2011 to do so. The Department of Transportation (DOT) failed to meet that deadline again and again and again. Only in 2014, after a lawsuit that my organization initiated, did the agency finally establish a deadline, and we will now in 2016 now have mandatory backup cameras going forward. The cost of that delay is hundreds of lives, mostly children, and tens of thousands of injuries that could have been averted.

My second example, in the area of interest to many on this Committee, is oil trains, where the rulemaking process has been appallingly slow. Members on both sides of the aisle have complained about it, and that is not just an accident because the agency is inept. It is because of the rulemaking process itself.

A second area of concern is weak enforcement. If we have existing rules, they ought to at least be enforced properly.

And a third area, which I will just rush through because I am running a bit low on time, is the use of cost-benefit analysis moving beyond as an analytic tool but to the decisionmaking criteria has led to an industry slant that is now, I am afraid, characteristic of the entire rulemaking process and itself has infiltrated the judiciary.

My third and final point, this Committee has been a welcome exception to much of the partisan divisiveness over the regulatory issue, but I do think there are areas of common ground for this Committee and others to explore.

The first thing, in my view, should be the failure of agencies to adhere to statutory mandates. If Congress gives a deadline, the agencies ought to take that seriously. They do not, and no one in Congress should accept that.



Second, there is a huge problem in a number of agencies with revolving door, people going into agencies, out of agencies, and into regulated industry. I think that is an area where there can be common ground. I know there is interest on that issue in this Committee.

The third area to look at would be proper regulatory enforcement. As I mentioned, we have—and partly it has to do with regulatory budgets, but agencies are not able to enforce the law properly.

And as a final point, I think there ought to be more attention to how regulations can advance the interests of small business and especially promote market competition. Markets do not actually just happen on their own. They require appropriate rules. And in the absence of intervention from the government to assure fair market competition, we see too many oligopolies and monopolistic practices in the marketplace.

Thank you very much.

Chairman JOHNSON. Thank you, Mr. Weissman.

First of all, nobody, I think, argues that you do not need regulations, or government, it is a matter of over-regulation, regulations that create a great deal of uncertainty, and that is—what is happening right now is this massive government is flooding the zone and it is almost impossible to comply with everything. There was a book written, what is it, *Three Felonies A Day*. You end up not a Nation ruled by law when you have so many laws, so complex, enforced at the discretion of prosecutors and regulators. I mean, again, it creates such a high level of uncertainty.

For example, with the net neutrality rule, it is dampening investment. It is a real concern. We saw over-regulation in Europe, investment in the Internet declined.

Professor Turley, I want to talk—because you were exactly right. Congress has given away its authority in so many areas. Here is an example, and I realize these numbers are always subject to dispute, but it gives you some indication. When Obamacare was passed, there were 380,000 words—I use words, because page count is different. Dodd-Frank was 368,000 words. Now, these are not exact numbers, so a caveat when I get PolitiFact checked on this. Obamacare now is approaching 20 million words. Dodd-Frank is somewhere around 15 to 16 million words.

Who is writing that? It is certainly not Congress. So, Congress passes frameworks and basically, for a host of reasons—you mentioned the Chevron decision—just giving all of the authority to the agencies. It is giving it away. And, of course, the agencies have definitely accepted it.

So, I want to talk a little bit about—you talked about the Administrative Procedure Act, which is supposed to try and set up a process for rulemaking that involves the private sector. What can we do to strengthen it, because if we do not catch it on the front end, the legal system is the only recourse, and I want to talk a little about that. But, let us talk about what we need to do on the front end, maybe at the Administrative Procedure Act, to prevent this type of fourth branch of government taking over this Nation.

Professor Turley, can you speak to that.

Mr. TURLEY. Thank you, Mr. Chairman. I think that the two things that the Senate needs to keep in mind is that, first of all, the APA was never designed to be an alternative to the democratic process. It was never designed for that function, but it is functioning that way. It is functioning as a governing system. People elect you. They believe that you are the ones that write laws. But, I think we all recognize that is really not the case. You actually write a very small fraction of the laws that affect most people.

So, partially, which I believe is important, is that this Congress has in the past tried to pull back a more active role when it comes to major regulations. I think that is a very good idea, as I say in my testimony.

The second thing is I think the Congress has to be honest about what is sort of a noble lie. The APA talks about the public participating in the regulatory process. If you take a look at some of our recent controversies, like the one that was just heard in the Supreme Court involving immigration, the administration asked for changes from Congress. Those changes were not given by Congress. And then the administration just declared them general statements of privacy and not only ordered them unilaterally, but did not even satisfy the notice and comment period.

And if you take a look at the net neutrality controversy, no matter how you feel about net neutrality, you cannot possibly believe that that is a good process for the American people. This is a huge issue involving billions of dollars. Millions of people are relying on it for communications. And yet it is this opaque system where rules change in short order and you can see the total disregard of the notice/comment period under the APA.

So, I think that the most important thing for this body to recognize is regardless of what comes out of this, the APA is not functioning the way it is supposed to function and this body needs to be more active in the lawmaking part of this administrative state.

Chairman JOHNSON. So, again, kind of new on the scene, here for 5 years just watching this, not being an attorney, I am seeing the APA as a potential check because it is being violated. It is being ignored. Tell me how effective it has been in terms of court challenges when the administration violates it.

And how long it takes.

Mr. TURLEY. Well, I do not mean to laugh, but if it was not so sad, it would be a laughing matter. I mean, as a litigator, going forward on an APA claim is truly a quixotic endeavor. The agencies require very little for agencies to satisfy the APA. You have to allow for the notice and comment period. That is what was so shocking about *United States v. Texas* is that they were actually circumventing what is the least burdensome requirement in government.

But, in reality, agencies are often criticized for reaching a conclusion and then sort of having this sort of Potemkin village of the appearance of participation and then issuing largely those same results.

In my view, the APA serves very little in terms of public benefit, but when you go to court, as long as they check off those procedural requirements, which are a minimum, you are pretty much done. I mean, the courts do not really get into this very much.

Chairman JOHNSON. So, if you get an injunction against a particular executive action because you have not followed APA structure, you are really ignoring the will of Congress, basically, is that right?

Mr. TURLEY. Yes.

Chairman JOHNSON. Mr. May, I want to talk a little bit about the independence of an agency and the FCC. Now, in our report, it is pretty shocking. Supposedly an independent agency. You take a look at the timeline of where the FCC was going in terms of their open Internet rule and how they turned on a dime in reaction to President Obama's statements on where he wanted to go with the regulation of this. Can you talk about how important it is, having been part of the FCC, to actually have an independent agency independent of the administration? Actually, by the way, the FCC is accountable to Congress, not the administration.

Mr. MAY. Thank you, Senator Johnson, and thank you, by the way, for the report that the staff issued, because I know it is not easy getting that type of information, I assume, from the Commission, with those e-mails. But, they were useful and the report was very helpful and illuminated—

Chairman JOHNSON. It is a little bit like pulling teeth.

Mr. MAY [continuing]. Well, I have tried to pull a lot of teeth over there in the last several decades. But, anyway, thank you for the report.

The question of the agency's independence, like a lot of these things, some of the lines are not hard and fast where you could draw a bright line. And to be honest with you, this process was troublesome, as I am going to explain. We are waiting for a D.C. Circuit decision that could come down any day on the FCC's net neutrality rulemaking, so I am a little reluctant to say exactly what the FCC did as, unlawful, because maybe, unless the Supreme Court comes up, who knows what the court will say.

But, here is the problem in this particular case. First, the way that the President intervened was much different and more high profile than anything that did occur, previously, in my experience, long experience. And by that, I mean, typically, the administration would submit comments during the comment period, this is our view, or write a letter, and there is nothing improper about that in terms of compromising the agency's independence.

In this case, what happened, the President released a video and a statement and it said in there, there is a bit of a wink and a nod, I know you are independent, but I am specifically asking that you take this course of action, which was the title to the public utility regulation. And then there is, as you know from what you uncovered, the staff had already prepared at Chairman Wheeler's direction a draft notice which went in the other direction, the more light handed regulation, just to simplify it.

Well, within days, they were directed to start drafting another notice which did specifically what President Obama asked them to do, and they did not issue a further notice seeking public comment.

Now, another thing that makes that problematic is that in the original Notice of Proposed Rulemaking (NPRM), which had probably 500 questions in the notice, there were only two paragraphs

that were exploring—that asked about taking this Title II approach and, gazillions of others about the other approach.

So, when you put that all together in terms of the context of what happened, it does give the appearances that the agency's independence was compromised, and without doing an administrative law lecture here, the idea of these independent agencies like the FCC and SEC and the Federal Trade Commission (FTC), as you know, when they were set up, it was to be—they have multi-member commissioners, staggered terms, fixed terms. All of that was to give them independence that is different from the Executive Branch agencies. The President can tell the head of EPA to do whatever he wants them to do. If they do not do it, he can fire them. That is not the case with the FCC's Commissioners.

So, when you have the context and you put it all together, what it does, I think, at bottom, as I said in my testimony, it jeopardizes the appearance that the FCC is independent and is acting on the basis of political considerations rather than on the basis of, its expertise, which as Professor Turley knows, of course, was the premise for establishing these agencies.

Chairman JOHNSON. Well, it is pretty obvious they were not acting independently.

You said it is very difficult, it is like pulling teeth to get information. We have yet to get that draft open Internet order—

Mr. MAY. Can I just say one thing?

Chairman JOHNSON [continuing]. Or that draft Public notice. We cannot get it. Kind of, why is that?

Mr. MAY. Just very quickly, I mentioned the high profile nature of this intervention. What is disturbing, too, is that the President also intervened in the same way in what is referred to as the municipal broadband preemption proceeding, and just last week, there is this very controversial proceeding, a lot of problematic areas about set-top box regulation, where the market seems to be working, really, fine. It is very dynamic. And he came out and essentially took a very specific position in another high profile way. And, so, I am worried if we see this become the pattern or the norm rather than historically what happened was he would file comments through the National Telecommunications and Information Administration (NTIA) in the FCC's proceeding.

Chairman JOHNSON. Well, one thing I entered into the record here, this 1991 Office of Legal Counsel letter on ex parte communication. I mean, here is the quote. "White House staff members should avoid even the mere appearance of interest or influence, and the easiest way to do so is to avoid discussing matters pending before the independent regulatory agencies with interested parties and avoid making ex parte contacts with agency personnel." I would say President Obama kind of talked about it. Senator Heitkamp.

#### **OPENING STATEMENT OF SENATOR HEITKAMP**

Senator HEITKAMP. Thank you, Mr. Chairman.

I would suggest that we be a little careful on how we define ex parte contacts, given that every one of us comments to agencies and calls them in during their regulatory process, whether it is DOL or whether it is EPA. So, we need to be a little careful, be-

cause if you are worried about ex parte contacts, that could be not just the administration——

Mr. MAY. But there is a specific——

Senator HEITKAMP. I have a question. Mr. Kovacs, thank you so much for your comments, because I think that you hit the nail on the head, that this is an abrogation. This is Congress saying, these are too tough for us to deal with. We cannot find common ground, so we would rather rail at the administration, we would rather rail at the agencies that draft these rules, which, oh, by the way, they are going to reflect the politics of whoever sits in the President's chair who appoints the person who sits at the cabinet table.

So, we own this problem, in my opinion. We do not do things—and I go back to judicial review, and you said very seldom does this happen. *Waters of the United States* is a failure of judicial review to provide clear guidance. They have rejected the EPA definition not just once, but twice after very costly litigation.

So, if I am going to solve this problem, what I am going to do is I am going to legislate. I mean, that is where we get into all of this discussion about railing against administrative agencies like we have no control.

And, I would say, when we start out a sentence with, because of regulation, we are safer, regulation is done at the direction of the Congress. It should be because of legislation, we are safer, and we have not done what we need to do to be clear in legislation. Therefore, it takes hours and days, and you can criticize the length of the process, but I have a certain sympathy for agencies who cannot seem to get that work done when we have given them no resources to do it and these are such tough issues, we have dodged them, whether it is an issue of regulation, whether it is *Waters of the United States*.

And, so, there are two issues here. No. 1, dealing with, I think, Mr. Kovacs, you talked about that small percentage of rules which really lead to a lot of the controversy and really having Congress take a greater role in analyzing those, but we should be here talking about APA changes, and we have had a number of discussions in the Subcommittee about what those changes should be, whether it is retrospective rulemaking, taking a look.

We have some great legislation. Senator Portman has some great legislation on independent agencies. We think that we have done a pretty good job taking a look at appropriate pre-warning, whether that is Advanced Notice of Proposed Rulemaking, which has been criticized by the left because somehow they think that they do not have access to the same process, and depending upon who is sitting in the White House, we get different perspectives about what the overall process should be.

I, personally, believe we need to amend the APA. We need to have a discussion about Advanced Notice of Proposed Rulemaking on major rules. We need to talk about what independent agencies should be required to do in terms of cost-benefit analysis, and for the life of me, I do not know—we are in a big debate about how we say that, right? I mean, that is the absurdity that we are at here.

And, so, on all of these issues, if we could find common ground, I think that—and set a new path for amending the APA in areas

where we can all agree, which I think there are, but we way too often criticize regulatory agencies when the criticism really should be back at Congress for failure to respond.

So, if you had to list the ten rules from your perspective, Mr. Kovacs, what would be those ten rules that you think Congress should legislate a solution to?

Mr. KOVACS. Well, you can take—here is what the difficulty of taking ten rules, and there are. I could go through ten.

Senator HEITKAMP. Yes.

Mr. KOVACS. You go through Waters of the United States, you go through clean power, net neutrality, set-top boxes. I mean, we probably—

Senator HEITKAMP. Yes. DOL—

Mr. KOVACS [continuing]. If we sat around—DOL—we would probably all come to an agreement on what they are.

You hit the nail on the head when you said Congress needs to amend the APA. That is the bible of the administrative state, and you need to, frankly, tell the agency, you have to check off this box, this box, and not just check off. If it says you have to talk to small business and see if they are hurt, they really have to talk to them. They cannot just check it off and say they are not here.

The other thing is, by doing so, you give the court clear standards for review, which the court does not have. So, right now, the court is looking at two or three million pages of a record, and in that record they are saying, we do not know what the science is. We do not know what the economics are. We are going to give deference to the agency. It is really up to Congress to say, here is what we want the agency to do to get to this, because after all, the goal of all of this is to get a rulemaking that implements what Congress wants done. And then the court needs to be able to look at that in a very strict way, not just with general deference.

And that alone for those 5, 10, 15, 20 rules, you really only probably get five or six a year, and the agencies can handle that, because they have 4,000 rulemakings and you are asking them to do more. And the best example is, I think it was about 10 years ago when the Occupational Safety and Health Act (OSHA) did ergonomics. The OSHA system is something you should really look at, because their on-the-record rulemaking, some of the opponents of it would say, well, it takes too long. They did the entire ergonomics rule, which is a multi-billion-dollar rule, they did it in less than a year. They did it faster than if you were going to have—if you were going to go through the informal process where you take in millions and millions of comments.

But, the other thing that is really amazing about it is they give a record that a court can review. Courts understand findings of fact and conclusions of law and the agencies have to give it to the records, and that is—Senator Portman's bill does a lot of that, to get you to that point where a court can actually review it.

Senator HEITKAMP. Yes. I think the interesting thing is that if we had a Republican administration, the dialogue might completely shift between what the Republicans are saying and what the Democrats are saying, and we cannot have that kind of political roller coaster based on who is sitting in the White House. We have to have rules of the road. Policies will change based on who is run-

ning the Congress. Policies will change based on who is the President. But, there should be a baseline, and I think we have lost, I think, a lot on both sides feel that that baseline has turned into quicksand. We do not know what the rules are anymore and we do not really have an independent place to go to get evaluation and analysis.

And, so, we are going to continue to work on systemic changes. I am going to continue to work on legislating on Waters of the United States, because I think, ultimately, after, what, at least 20 years of litigation in the Supreme Court, we ought to take some responsibility for the definition.

But, I really believe that this should not be as partisan as what it is, that we really ought to have an opportunity to have a broader conversation, and I am going to keep pushing for that here.

Mr. KOVACS. Thank you.

Senator HEITKAMP. And, really appreciate your testimony. We really appreciate the work that you have done, the effort to kind of analyze this from, I think, a politically neutral kind of standpoint, because to me, this is not a political issue. This is about what are the rules, how are we going to evaluate whether people are complying with the rules, agencies are, but how are we going to better evaluate Congress's failure to provide greater guidance in all of this, thereby enabling agencies to legislate—in fact, not just enabling, requiring agencies to legislate. And, so, these are problems that we should not look at through a political lens.

So, thank you, Mr. Chairman.

Chairman JOHNSON. Thank you, Senator Heitkamp.

And, by the way, I am surprised that it is partisan. I mean, let us face it, every one of us who serve in this body meets multiple times a day with groups coming in, business groups, universities. They all complain about the same thing and they are all asking for relief from the regulatory burden here. So, it surprised me we could not put together our relatively modest little package of regulatory reform bills, have a process of subtraction as opposed to addition, but we were not able to do that, so let us continue to work with you and Senator Lankford and your Subcommittee to make this a nonpartisan issue and actually get some reform. Senator Portman.

#### OPENING STATEMENT OF SENATOR PORTMAN

Senator PORTMAN. Thank you.

Now that she is leaving, I can say good things about her. [Laughter.]

As a Republican, she might not want me to say, but what Senator Lankford and Senator Heitkamp have done in the Subcommittee is extraordinarily good work, in my view. One of the things Mr. Kovacs has spent a lot of time on, as you know, is the Regulatory Accountability Act and how do we reform the APA for the first time in 70 years. I mean, think how the world has changed since then, how much more complex the issues are we have to face.

And the reality is, yes, Congress has not legislated in a way that gives the agency the guidance that they need, and it is partly because of the complexity of the issue, whether it is with regard to net neutrality or Waters of the United States or the fiduciary rule

or health care, and as a result, we need to update the APA. I mean, it is well meaning at the time, but I do think we have the right balance with regard to the Regulatory Accountability Act. It is bipartisan. It has been from the start. It has passed the House a few different times already. And it is the one broad sweeping bill.

I want to thank Senator Johnson, because as Chairman of this Committee, he has tried to push these regulatory issues where we can find common ground, not to say we are going to go with the Regulations from the Executive in Need of Scrutiny (REINS) Act, even though there are lots of Republicans who support that, but how do we find something that can actually find common ground, and I think the independent agency part of the Regulatory Accountability Act is one of those relatively small bills that we should be able to get done, even in this environment. We have not been able to yet. But, I do think that the Regulatory Accountability Act is going to help to solve some of these problems.

And, I would just ask you an interesting question right now, because we are in the middle of all of these very troubling rules. I was on a dairy farm over the weekend in Ohio talking about Waters of the United States. You can imagine this dairy farmer, who is struggling to try to keep the narrow margins that he has, looking at his ditch that only fills up in the spring with water and he is wondering whether he is going to have these costs imposed on him if he wants to develop that area or put a bridge across it or whatever. The EPA itself, I think, has said that the average cost is going to be \$155,000 to alter a ditch on someone's property. He does not have that \$155,000.

But, in your written statement, Mr. Kovacs, you talked about that the real victims of the Federal administrative state overreach are not just these individuals like this dairy farmer, but also our States, because the States are being asked to implement sweeping changes without their consultation or support.

As you know, the Regulatory Accountability Act, which is S. 2006, you talked about, does not just update it. It ensures agencies are doing the legwork, have the transparency, have the meetings for the larger rules. As you said, there would be the kind of scrutiny you would expect to have with rules that have a greater impact at a public hearing, so there is a chance for a public administrative hearing to have these kind of points of view expressed.

Here is my question for you. If the Regulatory Accountability Act had been in law at the time when the Waters of the United States was going through the rulemaking process, do you think the rule would look different than it does today?

Mr. KOVACS. Well, it certainly would look different, just because of what the RAA would require. First of all, it would incorporate all of the provisions in the Executive Order, which brings in the cost-benefit analysis, the cumulative impact.

Second, it would bring in the concepts that are in the Information Quality Act, which gets to the connectivity of water. It would require that they go through and set up the Small Business Regulatory Enforcement Fairness Act (SBREFA) panels, which are so important, because they actually bring in and talk to businesses. It would actually require that they pull in the jobs analysis that the agency has been required to do for 45 years and has not done.



But, more important, what it does is it sets up the specific issues that a court must review. So that when EPA right now says there are no unfunded mandates because the State is going to do it and it is only a definitional change, check the box, its indirect effect on small business, EPA checks the box, the court is now able to review and say, did you do the kind of analysis on Waters of the U.S. that you needed, and had they talked to these various people, they would have talked to the counties and the counties would have said, my God, you have just made all of the ditches on the side of the road a tributary and do you realize it is—according to the Corps of Engineers, it is \$155,000 per permit? Well, how many hundreds of thousands or tens of thousands of miles are there of ditches? That is just one example.

They would have talked to the small businesses. They would have talked to your farmer and they would have said, well, we have a problem. Maybe you are going to exempt farmers from the dredge and fill permit, but do you realize when we apply pesticides, we are actually doing a discharge under the Waters Act. I mean, and they would have learned these things.

They went through the rule, saying it is a definitional change and we are not changing anything, and so it would have looked dramatically different, plus a better chance for court review.

Senator PORTMAN. I think you are absolutely right, and the court would have been able to review the actual requirements in the RAA, which would have given us the basis, should the administrative agency overreach, to be able to have a better chance of overturning it.

On the net neutrality rule, and I guess, Mr. May, you are the expert on that, I think it is another great example where if you had the RAA in effect, or even just the independent agency rule in effect, you would have a very different result. And, these numbers, but despite the President's Executive Order 13579, where he said that independent agencies should comply with the Federal agency requirement to propose and adopt regulations only upon reasoned determination that its benefits justify its costs, despite that, independent agencies often still do not do any cost-benefit analysis for major rules.

In fiscal year 2014, only one major rule out of 17 issued by independent agencies included a complete monetized cost-benefit analysis—only one. And if you look back over the last 3 or 4 years, the record is no better.

So, my question to you is sort of the same. This is an independent agency that did not follow this. If they had undertaken a more thorough cost-benefit analysis, what would we have ended up with? Would we have ended up with a better rule?

Mr. MAY. The short answer is, yes, we may have ended up possibly with no rule, or almost no rule. There are aspects of it which might have still some relevance.

But, I think to illustrate this in a way that paints the picture, in the final order, the FCC—it was all put in conjectural terms, what might happen, could happen as opposed to any type of rigorous analysis. We counted over 250 times in the order where the FCC said this could happen or that might happen, as opposed to detailing evidence of incidents, other than a few. There are about

four acknowledged instances that happened that could be net neutrality-type violations that were quickly remedied.

So, essentially, I do not think anyone argues there was a cost-benefit analysis. Presumably, had there been one, the FCC would have determined that the rule was not needed, or perhaps this FCC might not have, but then a court, at least, would have had a record that would have been one that would have allowed it to review, really, the costs and benefits.

Senator PORTMAN. Yes. And, judicial review of everything on the private sector side, and yet with these rulemakings, not having that judicial review is obviously a huge problem right now with the overreach.

I am going to submit some more questions for the record to you, Mr. Campbell, because I agree with you on the fiduciary rule, and I also, sadly, having been at the Department of Labor and seeing this, you understand the impact, which is going to be keeping small businesses from having a plan. I think this is overreach into the IRAs. If you look at where their jurisdiction is, typically, it has been with regard to plans, company plans, and I think there are other concerns about the final rule, as well, that I am very concerned about for low-and moderate-income savers.

But, I will be submitting some questions to the record for you. I hope you will be able to respond to those quickly and we will be able to better get those out.

Mr. CAMPBELL. I look forward to it and be happy to, sir.

Senator PORTMAN. Great. Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you, Senator Portman. Senator Ayotte.

#### **OPENING STATEMENT OF SENATOR AYOTTE**

Senator AYOTTE. Thank you, Chairman.

I want to thank all of you for being here today. I, too, am an original cosponsor of the Regulatory Accountability Act. I would love to see us pass that and the REINS Act and many other efforts to reform this process.

But, I have to ask, where do we fall in this, because it seems to me that we pass a lot of laws and we give the discretion to the agencies. I can think of many examples. I was not here when the Affordable Care Act (ACA) was passed, certainly, but there are more "Secretary shall" in that. But, that is not the only piece of legislation that we can get that example. There is almost every major piece of legislation, we defer major decisions to these agencies.

So, do we not have a part in this? Should we not be looking at more tighter drafting of the statutes that we put forward? Mr. May.

Mr. MAY. Yes. Now, of course, it is true—I think Mr. Kovacs said, Congress cannot legislate all of the details of all regulatory programs. That is true. But, you can be more specific in some cases. I am going to give you an example from the communications area that I practice in. I know you are familiar with it, as well, from your Commerce—

Senator AYOTTE. Commerce Committee, yes.

Mr. MAY [continuing]. Committee perch. But, the Communications Act, as you know, delegates to the FCC the authority to act, “in the public interest,” actually 110 times in the Communications Act. You can see I have done a lot of counting of these things. But, to my way of thinking, going to Professor Turley’s point, number one, if I were on the Supreme Court, that would be unconstitutional because it is a meaningless delegation to go act in the public interest, but the Supreme Court has——

Senator AYOTTE. Fairly broad, as you can imagine.

Mr. MAY. Yes. I mean, the real definition of that is it means whatever three of the five FCC Commissioners say it does on any given day, and that is the truth.

So, here is a concrete example, because I do have my communications expertise, and then I want to make one administrative law point. So, there is talk about rewriting the Communications Act, and when you think about that and when that is ultimately done next time, the Congress should specifically in the legislation include a requirement that FCC decisions should take into account marketplace competition and consumer welfare. Now, that sounds—I mean, that is typically what you are trying to figure out when you are thinking about legislation, but in the Communications Act, you have the public interest delegation rather than marketplace competition.

But, the other thing I would say, really, is that it is important—so, Congress should legislate more specifically sometimes. But, the bills like the Accountability Act and things like that that at least focus attention on the major rules of economic significance, how those are defined, I mean, I think it is important that that type of legislation be passed so that at least the rules with the major impact can, in one way or another, receive more attention.

Senator AYOTTE. Mr. Campbell, I know that Senator Portman touched briefly on the fiduciary rule that has been issued by the Department of Labor. The first reiteration of the rule also included Employee Stock Ownership Programs (ESOPs), and I helped lead the effort to get the ESOPs out of it because it would have really undermined, if not destroyed, that model of employee ownership. So, we were able to get some traction there when they reissued the rule.

But, on the latest version, I share many of the concerns that Senator Portman has raised, and, in fact, last month, the Senate Banking Committee held a confirmation hearing for two SEC nominees and both nominees commented that they were concerned that the fiduciary rule would make it harder for American families to plan and save for retirement. But, because the rulemaking process, to a large extent, there have been lots of comments submitted, and I have not just had this experience with the fiduciary rule, but where you have a whole host of comments that are submitted from a wide variety of stakeholders and they seem to be pretty much ignored.

And we now, I think, also are seeing it with some of the new rules that DOL has issued on overtime. I have nonprofits in my community. Literally, my nonprofit community has been going crazy, saying this is really going to hurt our ability to serve our constituents.

So, I would like to get your comment on the fiduciary rule, but what about this comment process in general, which seems to be largely ignored, as far as I can tell. There is once in a while where you can get a good example where they are taken into account, but for the most part, I do not see the comment period as—even when people legitimately participate in this process—having a lot of interest from the agencies issuing it really taking these comments in full consideration.

Mr. CAMPBELL. Well, I think you make a very important point, which is the power of an agency to proceed with its own policy judgment is relatively unconstrained, provided they check the boxes on the processes they go through, and one of those boxes they check is we made an opportunity for public comment. We looked at the public comments. We may not have taken any of the public comments, but we did take them and we did look at them. And, that is an important distinction between actually being informed by them, learning from them and adopting changes in response.

I think the fiduciary rule is a particularly egregious example of this in how rapidly they went through this process compared to the normal Department of Labor process for considering comments. They closed out the comment period on September 24 on the most ambitious regulation making the most changes, I think, in the history of the agency. I think that is a fair assessment of the scope of this rule. And, yet, by the end of January, roughly 4 months later, they had completed a final rule, adopted a final economic analysis, and sent it to the White House Office of Management and Budget for review. I do not see how they could have done a truly credible job of considering those comments in that period of time given the scope of the comments and the number of issues in that rule.

Senator AYOTTE. Thank you, Chairman.

Chairman JOHNSON. Thank you Senator Ayotte.

Let me go right to what happens legally—I will go to you, Professor Turley—when an agency checks the box, gets the comments, potentially in some of these cases tens of thousands of comments, and just completely ignores it. Does that set up a legal challenge? Does that help them in any way, shape or form? Or because of the Chevron decision, it does not make any difference?

Mr. TURLEY. Well, I think that is—you put your finger on the main problem facing citizens when they try to get responsive action from agencies, is that they run into this truck called Chevron. And, Chevron affords sweeping deference to these agencies. The courts are not going to sit there and say, did you really listen to them, or did you sort of listen to them. As long as they went through the procedural requirement, the courts removed themselves.

And, the courts have adopted standards which I find are just completely unintelligible. The greatest example is that the court has said that while Congress cannot delegate its core authority to an agency, it can give directions as long as there are intelligible principles. But, that standard is actually unintelligible. There is no there there.

Chairman JOHNSON. Well, I was expecting Congress to do so. [Laughter.]

Mr. TURLEY. And, so, what happens is that you get to these courts and the courts will accept most anything as an intelligible principle coming from Congress, including these broad provisions that we talked about earlier with Randy, and you get hit on both ends. They get huge amounts of deference under Chevron and they also have these procedures that are very easy to satisfy, but they give nothing to people in reality in terms of consideration.

And, what is happening then is that the center of gravity of the legislative process has moved into these agencies and these systems are really a Potemkin village. They give the appearance of listening to citizens, but these agencies have the ability to dictate exactly what they wanted originally, as long as they tell the courts, yes, we listened to them and it turns out we were right all along.

Chairman JOHNSON. So, from what I have witnessed, it seems like the main benefit of the comment period is if the public floods an agency with comments and they are all pretty much on the side against the agency, there is a political effect of that, and sometimes agencies back off. But, when you have an administration that says, I do not care, push through, there is really no legal redress.

Mr. TURLEY. There is not, and one of the things I suggest is that Congress can take on Chevron. I mean, Chevron, once again, is being treated like it is a fixed part of our system. It is not that old. And what preceded Chevron, the Skidmore standard, was not particularly onerous for agencies, but it did allow courts to take a serious look at what these agencies were doing.

Congress actually can take measures to curtail Chevron, and one of them is to get a handle on this non-delegation debate by making it clear—I suggest a Chevron provision making it very clear that courts are not to give that degree of deference in various areas.

Mr. MAY. Could I add—

Chairman JOHNSON. Mr. May.

Mr. MAY [continuing]. A quick word. I do not know whether Professor Turley will agree or not, and I do agree that taking Chevron is good, but as a lesser included step, I think Congress could say the independent agencies, like the FCC, are not to be accorded Chevron deference even if the executive agencies are not addressed, and the reason for that is when you look at Chevron, the primary rationale for the Chevron decision was that when Congress leaves an ambiguity, that you should look to the administration and the President. I think the Chevron decision refers to deference to the administration.

Well, in line with what we have been talking about, the independent agencies, whatever their relationship to the President, is not the same as the Executive Branch agencies and there is a good argument that they should not receive the same degree of Chevron deference. Elena Kagan, now Supreme Court Justice, she in this law review article, long law review article she wrote when she left the Clinton Administration, she basically agreed. I have written two articles on this myself, but she agreed that because the independent agencies are not supposed to be subject to the same direction of the President, they should not receive the same Chevron deference.

So, in my written testimony at footnote 27, I cite two of my articles on this point about Chevron deference, and I do think it is worth looking at that discrete issue.

Chairman JOHNSON. OK. Go ahead, Mr. Campbell.

Mr. CAMPBELL. If I may, sir, I would say, though, that the comments, while they have very little effect in blunting a major policy or political view of an agency, do often have a significant effect in changing technical application. So, it is probably, in fairness to the agencies, the comment process is still useful and still something that we certainly want to preserve, because that does—

Chairman JOHNSON. When it is not ignored.

Mr. CAMPBELL. When it is not ignored, which it typically is not on purely technical matters, but those often are quite important and would be expensive if they were done incorrectly.

The other point I would make is while I agree that Chevron deference creates some significant concerns, I also think in looking at this as a matter for Congress to consider, how would you rewrite the law to address that, I would not want to create the same problem in reverse with the judiciary. I would not want to have the judiciary able to second guess all of these decisions, as well, and replace an unelected, unaccountable bureaucrat with an unelected, unaccountable judge. I do not know that that is a good tradeoff, either.

Chairman JOHNSON. I think going to Professor Turley's point, that it really ought to be Congress that kind of is the melting pot in terms of settling some of these disputes. It is a far more democratic process than an agency or nine Justices of the Supreme Court.

Mr. TURLEY. Yes, and if I could add, and this follows up on what Randy said, one of the things, I think, that this body should seriously consider is also the city of Arlington case. When we are talking about barring Chevron deference, one of the more shocking things that has happened in the last few years was the Supreme Court saying that an agency would get deference even in interpreting its jurisdiction.

Many of us who have been critics of Chevron believe that was really the rubicon, that no matter how bad it might get, an agency cannot get deference in defining its own jurisdiction. It would become a perpetual motion machine. And, that is something I think Congress should make a priority, in establishing that it is not delegating the authority to agencies to make that type of decision.

Chairman JOHNSON. Mr. Kovacs.

Mr. KOVACS. Just to follow up on what has been talked about, are comments worth anything, the application of deference by itself is what allows the agencies overreach, because they know the court is going to go along with them unless they are absolutely crazy.

And, so, the advantage of amending the APA is that the Congress can set out clear standards for what the agency has to do as part of a rulemaking and the court has the ability to understand what Congress tells them to do so that they can be the kind of check on the agency power, because after all, in the end of the game, it is the court that is going to be looking at the record.

So, you need to do two things. You need to really, in my opinion, you need to, one, give clear standards for how the agency proceeds,

what they need to do, whether it be principles or not, and that helps the courts, because the courts are the ones that apply the deference. So, it is not just Congress. We are sort of beating up on Congress. But, it is Congress gave enemies broad laws, but the court gave enemies deference. Both the courts and the Congress walked away and said, let the agencies do it, and both have to begin to getting reengaged.

Chairman JOHNSON. I have a couple other lines of questioning, and one of the things I do want to do—just give you one thing to think about—I do want to go through these three examples, the costs and benefits, and Mr. Weissman, you can kind of chime in, as well, because we have been not asking you a whole lot of questions.

I want to quickly go back to Professor Turley, though. You talked about giving deference to the jurisdiction of an agency. Is that not really the definition of the Consumer Financial Protection Bureau (CFPB)?

Mr. TURLEY [Laughing.]

Chairman JOHNSON. No, I am dead serious about that. I mean, is that not a real problem with that particular agency, which I think a lot of us would say is probably just an unconstitutional agency because it has total deference over its own jurisdiction?

Its own budget?

Mr. TURLEY. Well, I find it very troubling, and as you probably know, the D.C. Circuit panel raised questions along these same lines, of what a strange creature this is to find within our system, where it seems to be not directly accountable, even for in terms of budgetary requirements, to any branch.

I find that deeply troubling. I do not have a dog in the fight in terms of the underlying merits of the Board. But, as someone coming from a constitutional standpoint, this is an entire different species. The Framers would not recognize creatures like this.

Chairman JOHNSON. I mean, what constraint does it have? I know it has a name and it is supposed to be directed there, but it can just about go anywhere, right, and there are no constraints whatsoever by anybody.

Mr. TURLEY. Yes, and I think I would beat up on Congress a little bit in this respect, and that is—

Chairman JOHNSON. Be my guest.

Mr. TURLEY [Laughing.] The thing is, members have been playing with their own obsolescence for years. It is very easy to create independent bodies to shove tough questions over there, and when things go wrong, you can criticize it. And the same thing is true with the President. It gives insulation to politicians that the Framers did not want. The Framers actually did not want you to be insulated in these respects.

And, so, that is why this whole system is becoming something other than what was intended by the Framers, and it is not a better system. I mean, that is what is interesting, is it is showing all of the dysfunctional problems that the Framers thought would occur.

And, when people say, well, this is an entirely different government, a different reality, it is not. I mean, the Framers were very familiar with giving authority to remote individuals. They called it

a monarchy. Now, we might have a technocracy, but it is the same concentration of power and it is removal from public influence and from public observation, and I think that is what we are seeing.

Chairman JOHNSON. Let us face it, Congress has been giving away its powers for decades. Power of the purse, you have two-thirds of the budget off-budget. So, much of the discretionary part is tied to mandatory spending, so the government shuts down and somewhere about 10 percent actually shuts down. Everything else just keeps moving forward. Advice and consent, it comes—executive agreements, we do not say, no, this is really a treaty. So, I am with you on that.

As a non-lawyer, I do want to continue down just the legal ramifications of this and how the courts tie into this. I want to talk a little bit about standing. You are aware of the fact that I tried to sue this administration to overturn a rule from the Office of Personnel Management (OPM), from my standpoint, clearly violated the very clear language of the Affordable Care Act in terms of allowing Members of Congress and their staff to have an employer contribution into the plans purchased through an exchange. I could not get standing.

Mr. TURLEY. Right.

Chairman JOHNSON. That is also a problem in terms of these other laws. Sometimes, it is just very difficult to even get standing to challenge. Can you just kind of talk about that issue.

Mr. TURLEY. Well, I am glad you brought it up. For one thing, it allows me to beat up on another branch, and that is when I look at the dysfunctional state of Washington today, I actually put the principal blame on the courts, not on the Legislative or Executive Branches. The reason is the courts have removed themselves from these disputes. Members like yourself have serious separation of powers questions to raise and courts say, I am sorry, we are just not going to let you be heard on the merits. And the result, then, is it reduces the two other branches to muscle plays. That is what we are seeing. But, it is that because those two branches are trying to fight for their institutional authority and no one in the court is giving them their day in court, as was the case with your lawsuit.

That is the reason for years I have argued that one of the great solutions that we could see in our lifetime would be to change standing, particularly to allow legislative standing. Members of Congress have skin in the game. They have important, particularly separation of powers, questions to raise. And I think that the court has made an utter mess of this area.

The standing doctrine itself, of course, does not appear in the Constitution. It is derived from Article III in terms of what is a case or controversy. But, the courts allowed the standing principle to become so grotesque that even Members of Congress that have legitimate constitutional issues, as was in your lawsuit, are not even being heard.

And, the reasons for that are really, in my view, implausible. It is, like, well, you cannot have all Members of Congress sue every time they believe that the President is acting unconstitutionally, and my answer is, why? Even if all of the members became litigious, it would be a drop in the bucket in terms of the number of cases that the courts deal with.



But, more importantly, members have the expertise, they have the perspective to raise separation of powers. And as someone who is a great advocate of a separation of powers doctrine, and admittedly, I am a formalist in that sense, we are at a new low in terms of the respect for the separation of powers and it is becoming more and more unstable.

I mean, when we talk, as you have said so many times, about Congress just basically relenting, one of the most bizarre moments of my lifetime is when President Obama stood in front of Congress and told them, I intend to circumvent Congress because you failed to do what I asked you to do with the ACA and other areas. Now, what followed was really otherworldly. Half of that body applauded rapturously at the notion of their own obsolescence, and that is something that Madison, I do not think, anticipated. He really did believe ambition could fight ambition when it came to institutional authority.

Chairman JOHNSON. Yes. The Members of Congress would actually hold their oath of office to support and defend the Constitution and jealously guard their powers, which is not happening.

I wanted—and anybody who wants to comment on this—I mean, another, I think, incredibly dangerous process is sue and settle, where agencies, again, the executive, you cannot get Congress to pass a law so they will work with an outside group, get that outside group to sue the government, and then the agency settles, and now you have a court sanctioned result, again, completely circumventing this body.

Does somebody want to speak to that? Mr. Kovacs.

Mr. KOVACS. Sure. Well, sue and settle is obviously one of our large concerns, but it also relates to your standing issue. For example, Congress has put standing issues—has granted zone of interest/legislative standing to environmental groups in 20 of its environmental laws. So, while you cannot get standing to argue separation of powers issues, the environmental groups get standing to protect their vision of what the forest looks like. So, that gets them into court.

And once they sue the agency, several things happen. The agency consents, and by consenting and going under a court order, the agency has now managed to make that issue a priority. So, whatever monies you appropriate, the agency takes and redirects them because they are now under a court order.

So, what happens is the environmental community is actually implementing their agenda through the sue and settle process, and again the courts—and we might as well just keep on beating up on them too—the fact is that the courts treat, sue, and settle, major policy disagreements like utility Maximum Achievable Control Technology (MACT) or the Chesapeake Bay, they treat them the same as if two private parties came in on a contract dispute and they just signed it and said, get out of my courtroom. They do not even look at the comments, if the agency ever takes comments. They do not look at them and they are not presented to the court. It is just, here is the consent decree, and they do it.

Chairman JOHNSON. When was the first time this was initiated, do you know?

Mr. KOVACS. Sue and settle?

Chairman JOHNSON. Yes.

Mr. KOVACS. That has been on and off for probably 20, 25 years. The only time it has really stopped between the Carter Administration and today was when Ed Meese was Attorney General (AG), and he had stopped it for a period of 4 years. Other than that, it has been continuous. The only difference is it was a few cases a year and a few cases within a term of the President, and I think in the first term of the Obama Administration, it was, like, 115.

And some of the courts, it is not just one regulation that they implement. One of the courts in the Northern District of California actually did 28 regulations at a time. I think that is the highest.

Chairman JOHNSON. Well, it has literally become the method of governing. Mr. May.

Mr. MAY. Mr. Chairman, let me just give you the FCC version of what you called sue and settle, and probably other agencies, as well. It is a big problem.

The FCC reviews mergers in the communications industry, as you know. It does it under the public interest standard that I have talked. In other words, that is what it is basing its decision on. Well, of course, that is indeterminate. So, what really happens, to make a long story short, is when companies have mergers pending before the FCC, before all is said and done, and that is usually at least a year after they file the applications—they end up coming forward and, “volunteering” certain conditions that, obviously, the FCC staff has communicated to them that they would like to see attached to the merger, but which may not and usually are not directly related to the specific competitive impact of the merger. In other words, they are other public interest types of things.

So, you end up with regulation by condition. That happens all of the time, and I believe that is probably the equivalent of what you are talking about with sue and settle, and that is an example, again, of something that could be corrected by Congress if it revised the part of the Communications Act dealing with reviewing transactions and just made more specific what the FCC should look at the specific impact of that merger and not unrelated issues in that proceeding.

Chairman JOHNSON. Does anybody else want to chime in on this one before I move on to the kind of cost-benefit? Mr. Weissman.

Mr. WEISSMAN. I think we probably disagree with you on this. I know we disagree with Mr. Kovacs. I mean, we view the, what is termed “sue and settle,” really as private enforcement, actually carrying out Congressional intent.

But, I thought it might be useful to step back to the standing issue, and I do not know that we would have agreement on this issue, but I do think there is probably agreement on the notion that there is a problem and that standing is far too narrow in too many cases. I mean, I think, interestingly, the environmental statutes are sort of unusual in granting a broader framework for standing.

As a consumer organization, we find when we are trying to enforce consumer or public interest in cases, we often do not have standing, even when industry might, and that there is a disparity there. Actually, sometimes industry has trouble getting standing, too, less so than us, but—

Well, he and I will have coffee and talk about it later. But, I think it is the case that the Supreme Court has narrowed standing in such a way that important disputes actually are not able to be adjudicated, and it is an area—it is a challenging problem, and Professor Turley is certainly more expert than me, because of the constitutional doctrine, it is not obvious to me how Congress can solve where the court is going with this. But, at least it ought to be scrutinized and we ought to be seeing—I think that we are seeing, actually, access to the courts as a means to resolve important disputes and even constitutional claims just being shut off because of an artificially constricted standing doctrine.

Chairman JOHNSON. I certainly learned that lesson myself.

Does anybody else want to chime in on this before we go into cost-benefit? OK.

Mr. CAMPBELL. I would just say briefly, sir, that I think there is a distinction between expanding standing to include Congress and expanding the standing doctrine generally, which I think is also an important tool preventing frivolous litigation.

Chairman JOHNSON. OK. What I would like to do is just, again, we have three test cases, and probably best to start with the potential cost and then talk about the benefit, and again, if that is OK with you, Mr. Weissman, it is kind of 3-to-1—

Mr. WEISSMAN. I think you get to decide that, sir.

Chairman JOHNSON. So, let us start with the potential cost of the net neutrality rule, Mr. May, if you would like to speak to that, or not.

Mr. MAY. No. I mean, I will, because I did during the proceeding. No. 1, I would just say at the outset, like someone else did, I am not opposed to all regulation or even all FCC regulation. But, in general, I do subscribe to the notion that if there is not a marketplace failure that is causing consumer harm, that is more than speculative, then you should be very careful about regulating, because cost—I mean, there is almost universal agreement among economists that costs do have an impact on economic activity. They tend to dampen investment. Now, that does not mean sometimes they cannot be outweighed by the benefits, particularly when we are talking about health and safety type regulation.

But in the net neutrality case, there was a lot of people urged the FCC, that if it adopted the rule, it would have an adverse impact on investment and innovation, and there has been—it is early, but there has been some persuasive evidence, I think, already that is beginning to appear that it is having that impact on investment. Hal Singer with the Progressive Policy Institute, not a free market type of institute, but he has done a study that showed that in 2015, there was a decrease in the amount of investment from the 12 largest Internet service providers of about a half of a percent, or \$250 million. That has an impact on, obviously, the jobs that depend on the investment, as well.

So, and I would just add that Commissioner Ajit Pai has identified, I think, eight different instances in which smaller Internet service providers have publicly said, announced, that they were cutting back on plans to increase their investment, as well.

Chairman JOHNSON. And, by the way, this is significant—because it sounds like a small reduction in investment, but the Inter-

net has been a huge boon to our economy, so there have been all kinds of investment on an annual basis. The only time we really saw a reduction, I think, was after the 2009 recession and after the dot-com bubble burst.

Mr. MAY. Yes. I mean, I think almost no one disagrees that since going back to 2000, there has been at least \$1.3 trillion of investment by the Internet service providers. Now, I am not talking about all of the other parts of what we call the ecosystem. I am just talking about the Internet service providers.

Chairman JOHNSON. Right.

Mr. MAY. And the only other thing I would add is you cannot—it is hard to measure the amount of investment that does not take place as a result. You try and do it, but it is not an exact science. But, again, it is widely understood that—

Chairman JOHNSON. Yes, that is why I said, the fact that it actually declined is pretty—

Mr. MAY. Yes.

Chairman JOHNSON [continuing]. Pretty significant versus it has always been growing. Mr. Weissman.

Mr. WEISSMAN. Well, just look again, just focusing on the costs, and, of course, I think the benefits are important, as well, I think that data is wrong. Broadband ISP investment is up in the year since the rule was adopted as compared to the previous years. ISP profits are up and stock values, for what that is worth, are up, as well.

I mean, I think one indication that the purported investment deterrence is actually not playing out and not nearly as significant at all as was claimed in advance of the rule is the distinction between what the companies have told—or said publicly about the potential impact of the rule in advance and what they have said in their SEC submissions, where they are required to be truthful. And, their SEC materials do not claim that the rule will have material harmful impact on them, and by and large say that they will be able to manage without any difficulty, and indeed, that has been proven true.

I think as time goes on, the idea that this was going to have such a huge cost on industry is just going to float away—

Chairman JOHNSON. So, again, you are disputing the cost, but what about the benefit? Why was this issued? What is the benefit of what the FCC is trying to do here?

Mr. WEISSMAN. Well, I think the benefits are enormous. The benefits are enormous, both on the consumer side—and, by the way, it has become a partisan issue here, unfortunately. It is not a partisan issue among the public, with self-identified conservatives overwhelmingly favoring what is called the net neutrality rule, and that is because it is essentially a freedom issue first. It has to do with whether or not there is going to be free, unfettered traffic, information exchange, over the Internet without toll keepers and without corporate sensors in the form of ISPs, and those are principles on which everyone should agree, apart from trying to monetize the value.

There are monetary benefits, too. There are monetary benefits to consumers in avoiding excess tolls that would have been imposed if the Internet moved in a different direction.

And beyond that, there are massive pro-competitive—pro-innovation benefits to the rule. There had not been a ton of examples of blockage, but there have been a number of important ones where we saw ISPs trying to deter the growth of Skype, deter the growth of Facetime, interfere with Voice over Internet Protocol technology.

And, of course, the Internet has been an area of massive innovation and expansion, but it actually—all of the apps that are going on, all of the innovation, it depends on the Internet being free, open, and unfettered, and not censored and not controlled. So, we are going to see enormous benefits. All the benefits we are talking about from the Internet actually would have been in peril if we had a whole different model of how the Internet was going to work.

Chairman JOHNSON. Well, it depends on investment so we can continue to increase speeds.

Let us talk a little bit about the fiduciary rule. Mr. Campbell.

Mr. CAMPBELL. Yes. So, the Department of Labor's rationale essentially is that securities laws are inadequate and that IRAs should be treated to a different standard, similar to employee benefit plans, and that as a result of that, there are conflicts permissible in the IRA space that would cost. And the estimates here became very difficult, frankly, I think, to agree with because they were pretty speculative. They were based on academic studies looking at one type of conflict and one type of product and whether this caused fees to be higher and returns to be lower, and I think it is very difficult to extrapolate that out. It also ignores an awful lot of other potentially positive effects that would go into that advisory relationship.

For what it is worth, the Department did revise its estimates in the final rule to reduce the benefits somewhat and increase the costs by a proportional amount rather significantly, I think probably still rather significantly underestimating the costs. Again, in my testimony, I gave an example of just the legal fees alone. They look at the cost for particularly disclosures that they are requiring and they assign a number of minutes they think it is going to take an attorney to write that disclosure, and then they assign an hourly value to that attorney's time.

And I gave the example, one of those disclosures, they thought would take 10 minutes to write. And at \$134 an hour, that would be \$22.33. But, if you get that disclosure wrong, you have potentially blown the exception and committed a violation of this contract, which is exposing you to a class action in State court over the entirety of your IRA business, which could be tens of billions of dollars. So, no one is going to spend \$22 to make sure that is right. They are going to spend whatever it takes to make sure that is right.

And that is just one example of the way they do these economic analyses, which are not rigorous and, I think, are not really accurate, reflecting reality.

Chairman JOHNSON. It is hard to monetize both costs and benefits, but I think it is pretty easy anecdotally to say they will not spend the costs. They will exit the business. I mean, is that not the real concern about the fiduciary rule, is people will just refuse to become a fiduciary because it exposes them to such enormous liability, they are just going to stop doing it, and so you have the

small to medium-sized investor that just will not have access to advice.

Mr. CAMPBELL. I absolutely believe it will reduce choices and increase costs, and that will drive some of these small accounts and small plans sort of out of the ability to get advice. I think it is less a question of driving service providers out entirely as it is imposing new costs and legal liabilities and ongoing compliance obligations on those service providers that make it unaffordable to serve small accounts.

So, it is not that they exit the business, going to the gentleman's point about the SEC filings, are these service providers saying, oh, we are just going to have to close up shop. No, but that does not mean they are not going to pay a lot more to provide a similar service and that that is going to hurt people.

Chairman JOHNSON. So, if you are a small investor, all of a sudden, you are seeing a cost of \$500 or whatever, you just do not access the service, so it is kind of the same thing.

Mr. Weissman, the benefit.

Mr. WEISSMAN. Well, first on the cost side, so the Department's cost estimate is really based on industry submitted data. It is one of the limits, by the way, of cost-benefit analysis. So, it is quite conservative and it really does rely on the framework that was provided by industry. They tweaked it around the edges.

They also, by the way, as Mr. Campbell pointed out, they made non-trivial changes even in this current version of the rule in response to comments about ways they could reduce costs.

In terms of the benefit, before thinking about the monetization, which—it is worth stepping back and thinking what the fiduciary rule actually is, which is a rule that requires investment advisors to have the interests of their customers at heart. That should not be that controversial. And, I think it is unfortunate that it has become so. And, it is for sure the case that consumers assume that that is the basis on which they are being served, even when it actually, it has not been.

Now, the benefit estimate—and actually, and that in turn makes a difference. If you have a duty to advance the interest of your customer, you do not layer them with all kinds of hidden fees that materially reduce their returns. So, the estimate from the Council of Economic Advisors is about \$17 billion a year annual savings from consumers as a result of the rule, and even that probably is a fairly conservative estimate, because they are only looking at a fraction of the accounts that would be affected.

Chairman JOHNSON. Mr. Kovacs, let us talk about Waters of the United States. I know in Wisconsin, we are looking at potentially more than 90 percent of the land mass of Wisconsin now being subject to EPA jurisdiction and permitting, the \$150,000 per permit, more than \$30,000 per day types of fines. Can you just talk about what you look at as the cost of the WOTUS rule.

Mr. KOVACS. Well, you certainly hit it. You described it perfectly. About 90 percent of the land in the United States would be subject to some form of EPA regulation, just because of the hydrology. It is \$155,000 a permit, and I do not know how many permits that people would need, versus highway administrations and farmers or

whatever. You would also need discharge permits. And you have the \$37,000 a day in fines, and fines goes up to a million.

So, let me read to you—because it is only a few words—what the EPA says is the cost of all of this. “The rule establishing the definition of Waters of the United States by itself imposes no direct cost.” Then it just dismisses it and says, well, “each of these programs may subsequently impose direct or indirect costs as they are implemented,” and, therefore, they just wipe away the theory.

And even on cost—and I am going to go back to unfunded mandates, because the States are really the ones getting saddled with this burden—if you went back to, I think it is 15 years, EPA issued 8,400-and-some rules and they only found unfunded mandates in 45 of them, and they only found that the States had to spend more money in five. So, it gives you an idea that whatever you are looking at in the cost-benefit is whatever the agency wants to tell you.

Chairman JOHNSON. And, of course, the Waters of the United States basically redefines what I think most of us would view should come under Federal jurisdiction, navigable waters, because if you pollute something in Wisconsin into the Mississippi, it affects other States. I mean, there is interstate commerce and that is reasonable. And it turns that into things like intermittent streams, playa lakes, which I had to look up in a dictionary. It is a bigger puddle. It is a puddle, but it is a big one. But, it probably does not define how big a puddle.

Again, Mr. Weissman, the benefit, then, again, recognizing the fact that we all believe that we want a clean environment and it is reasonable to have EPA jurisdiction over things like navigable waters, true navigable waters.

Mr. WEISSMAN. Absolutely. Well, if you will permit me, I think there is—Senator Heitkamp is gone, but there is a point that she was raising that is important, particularly in this area, which is there has to be a definition. The statute exists and there has to be a definition, and the EPA has to figure something out.

And they have been harshly criticized, by Chief Justice Roberts, among others, for not resolving a rule. So, the rulemaking had to occur. And, I think—because there had to be a workable definition. I mean, if you read the Chief’s comments on this, they are very harsh criticism. They have to establish what the scope of the Clean Water Act (CWA) is, and it has been murky around the edges as a result of the last two cases.

So, I think, before getting directly to the question, there really is a role for Congress to—you are not going to probably have that detailed a definition as EPA can possibly get, but you could go back and revisit it if it seems problematic.

Chairman JOHNSON. Well, by the way, they did try that, the Clean Water Restoration Act. It was not passed. And, again, it tried to redefine that and it was rejected. So, there was some definition that had been operating for a few decades, but go ahead.

Mr. WEISSMAN. So, in terms of the costs and benefits, so Mr. Kovacs read that excerpt which is correct, although the EPA—but, first, to explain that, the EPA said, look, it is definitional. All we are doing is creating a definition. They did not deny the definition would have effects. They are saying the fact of creating the definition itself does not have an effect.

Then they said, OK, let us go ahead and then figure out what the impact would be. And, they said, in contrast to what he has suggested, it does narrow the scope of covered waters compared to the statutory definition. So, they said, we could stop there and say it actually is going to have less cost than the existing statutory definition.

But, in fact, we recognize that it does expand around the margins compared to existing practice. And then they, therefore, did conduct a rough cost-benefit and say they believe the benefits will outweigh the costs by about two-to-one.

Chairman JOHNSON. OK. I will just quickly go down the table here. Does anybody have a final comment, something that you have just got to get out before we close the hearing? Let us start with you, Professor Turley.

Mr. TURLEY. Thank you, Mr. Chairman. What I really respect most about this Committee and your leadership is its interest in developing a nonpartisan approach to these questions, and I think what really comes out of this hearing—so, there are good faith arguments on both sides of these issues, but what we should agree on is the way in which we resolve these issues and for Congress to be relevant for that process. And, I do believe that the RAA is a good step. I happen to think that something like the REINS Act is a good step.

There is an assortment of things that Congress can do, and one of those, by the way, is also increasing its staff to specifically monitor in a more substantial way rulemaking. We have not talked much about that, but part of the advantage the administrative state has is that its sheer size overwhelms Congressional staffers. And, so, this almost becomes arbitrary as to what issues can first come to the attention of Congress and what issues can be addressed.

Congress has no choice if it is going to be relevant to get some boots on the ground, to actually have, what I recommend is an actual office that will be looking at rulemaking so that members are not in the blind. And, I think these are the types of steps that I hope members can agree on in a nonpartisan way, that they should be informed, they should be more involved, and they should fulfill what is probably the sacred function of our Constitution. That is, this is the place where the country has to resolve its disputes. It does not always resolve it. Sometimes, the country is terribly divided, and then less gets done. But, this is the place where the Framers wanted those questions to be resolved and I think we have to move back in that direction.

Chairman JOHNSON. We have been trying. Mr. May.

Mr. MAY. Thank you, Mr. Chairman.

I would just say this in closing, that the FCC, unlike the other two agencies of the case studies, is considered one of the independent agencies, as we have discussed, so that makes it different.

I mean, I will say that the whole nature of independent agencies under our tripartite system of government, constitutional system, is a little uneasy, but once we have them set up as they are with the notion of independence, which we do, at the core of that is the idea that they will rely primarily on their expertise and not so



much on political considerations as might probably be the case with the independent agencies.

So, having said that, one thing that I—and we discussed this in the hearing, which I think was very useful, and thank you for that, I think it has been instructive. One thing I would like to see Congress think about is whether the Chevron doctrine which we have talked about here, if Congress does not change the law to even apply more broadly across all of the Federal agencies, whether it might be changed with regard to the independent agencies not to provide the same degree of deference that is provided in the other cases, and the rationale would be that these agencies are acting based on their expertise and not because of deference to the administration. Thank you.

Chairman JOHNSON. Thank you, Mr. May. Mr. Campbell.

Mr. CAMPBELL. Well, first of all, Mr. Chairman, I very much appreciate the work that this Committee has done, not just on this issue, but specifically on the fiduciary rule. The documents that the Committee gathered from the SEC, from the Treasury Department and other entities was invaluable in understanding what was going on, because no one but Congress would have had the authority to drag that out in that point in the process, so we appreciate that very much.

One issue I would raise that should be considered in part of regulatory reform is that there are a number of areas in the law, and employee benefits is one of them, where you have significantly overlapping jurisdictions of different agencies. So, you have the SEC, the Department of Labor, the Treasury Department, the Financial Industry Regulatory Authority (FINRA), all of these different groups simultaneously regulating the same activities, or at least aspects of those activities, and where those agencies do not effectively coordinate, the regulated community gets whipsawed in the middle.

And I think that is something that as the Committee looks at drafting, say, comprehensive legislation or considering one of the bills that is out there, that there be mandatory coordination between those entities so that we do not have one entity moving forward quickly, another not moving, and none of us knowing where we are ultimately going to end up.

Chairman JOHNSON. An interesting point. One of the hearings we are trying to design is get case studies where, to comply with this regulation, you are in violation here, and we know those exist and just kind of point out that enormous problem.

Mr. CAMPBELL. And the proposal for the fiduciary rule did exactly that. It required a disclosure that securities laws did not allow you to make. They did fix that in the final rule, but the fact that it was actually able to be proposed showed that they were not coordinating with the SEC and other entities in order to avoid such an obvious contradiction.

Chairman JOHNSON. Mr. Kovacs.

Mr. KOVACS. Well, again, I just want to bring up the fact that this Committee almost—not almost, it worked a miracle last year with permit streamlining. You were able to come together on an extraordinarily difficult regulatory issue and you came out with a great result, and we are working very cooperatively with OMB and

they have the cooperation of both the environmental groups and the business community.

This issue in terms of the regulatory State, this should truly be a nonpartisan, bipartisan issue. The importance is not to the Republicans or Democrats. The importance of this issue is to Congress. This is an institutional issue. You have to find and get back into what your role is. There is only one institution in this country that can delegate power, you delegate it to the agencies with guidance as to how you want the rules written, not specific guidance, but you have to take these things in to account, because after all, it is all about homework and getting it right. But, the guidance to the agencies also give clear standards to the courts so that they know how to review it, and that is why the Regulatory Accountability Act is so important.

Chairman JOHNSON. I appreciate that, and by the way, I appreciate you pointing out the fact that this Committee has really tried hard to try and find areas of agreement to actually unify us as a result. We literally passed 69 pieces of legislation, most of it unanimous, a lot of it bipartisan. I think it is 25 that have been signed into law. So, you actually can get a result by using that kind of approach. And, again, so these types of hearings—we are trying to, literally, ferret out and figure out where are those areas of agreement. Mr. Weissman.

Mr. WEISSMAN. A few quick points. One is I think we have had a lot of discussion about the difficulty of having court review of regulations. From our perspective, in fact, there is very intense and heavy court review of most regulatory decisions, a lot of cases brought by the Chamber of Commerce, unfortunately from our point of view, with great success. I think just the empirical record is the courts look at these things very carefully and routinely strike down rules.

A second quick point is there is more than a little bit of tension between the concerns about President Obama's alleged role in the FCC rule and sort of undermining the independence of the agency and the proposal of the Independent Regulatory Agency Review Act, which would actually make the agencies directly accountable to the White House itself.

A third quick thing, just to reference a point I made earlier that has been lost, I do think that there is a lot—it would be very fruitful for the Committee to look at missed statutory deadlines, sort of direct issue of accountability to Congress.

And the last point, just to echo some of these comments, whatever the differences are, I think everybody appreciates the tenor of the conversation in this Committee on these issues, no small part to your role, and we really appreciate that.

Chairman JOHNSON. Well, I appreciate that.

Again, reading through your testimony, I know you put a lot of work into it. I think it really helps inform the record, so I appreciate that time, the time you took here to testify, and again, great answers to our questions. I think we really helped this Committee understand kind of the direction we need to move.

So, with that, the hearing record will remain open for 15 days, until May 5 at 5 p.m., for the submission of statements and questions for the record.

This hearing is adjourned.

[Whereupon, at 12:10 p.m., the Committee was adjourned.]



# APPENDIX

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## **Chairman Johnson Opening Statement “The Administrative State: An Examination Of Federal Rulemaking”**

**Wednesday, April 20, 2016**

*As submitted for the record:*

Good morning. Thank you for joining us today.

In recent years, the size and scope of government has increased through federal regulations. As we have learned from small businesses and stakeholders around the country, overregulation is the silent killer of economic growth and opportunity. The purpose of this hearing is to understand the toll that excessive rulemaking has on our economy. We will look at three key issues:

First, we will examine the Obama administration’s use of the regulatory process. According to one study, since 2009, the Obama administration has finalized 588 major regulations—392 of which have an annual effect on the economy of \$100 million or more. Federal agencies have finalized an average of 10 regulations per day during this administration.

Second, we will consider the burden of regulations on the economy. According to some estimates, it costs Americans roughly \$2 trillion to comply with federal regulations each year. That is approximately 10 percent of the United States gross domestic product.

Third, we will look at the Obama administration’s approach to the regulatory process, considering three case studies where the committee has done oversight: the Federal Communications Commission’s net neutrality rule, the Labor Department’s fiduciary rule, and the Environmental Protection Agency’s “Waters of the United States” rule.

Last year, the White House pressured the FCC to reclassify broadband as a common-carrier—subjecting competitive internet services to the same restrictions as the non-competitive, monopolist phone companies of the 1930s or railroad companies of the 1800s. Private businesses now face significant uncertainty and compliance costs.

We will also examine the Labor Department’s fiduciary rule, which rewrites the compliance regime for retirement investment advisers. The rule will likely increase compliance costs for advisers, driving up the price of their services and decreasing access to advice for low- and middle-income investors. In drafting this rule, the Labor Department ignored concerns from Securities and Exchange Commission and Treasury Department staff.

Finally, we will examine the EPA’s “Waters of the United States” rule, which expands federal authority over small bodies of water that were previously not subject to federal regulation. Under the rule, 92 percent of the land in Wisconsin could fall under EPA’s jurisdiction. The rule threatens to harm Wisconsin farmers and businesses with increased permitting costs and litigation risks, including fines reportedly up to \$37,500 per violation per day. The Government

Accountability Office found that EPA engaged in “covert propaganda” in generating public support during the rulemaking process.

This hearing will further highlight the problem of unfair and unnecessary regulations and the cost to the American people. I look forward to your testimony.

**Opening Statement of Ranking Member Tom Carper**  
**“The Administrative State: An Examination of Federal Rulemaking.”**

**April 20, 2016**

*As submitted for the record:*

Good morning. I want to thank Chairman Johnson for holding this hearing today. My thanks as well to our witnesses for joining us. As many of you have heard me say before, I believe that one of the most important jobs Congress has is to help create a nurturing environment for job growth. And one of the ways we can do that is to ensure the regulatory process results in common-sense regulations that provide businesses with the predictability they need.

Of course, the regulatory process can be cumbersome at times. And regulations often do impose some additional costs and requirements on those who must comply with them. But I disagree with those who think that we have to choose between regulation and having a robust, growing economy. When done in a smart way, regulations can help grow our economy. Regulations also serve a number of very important public purposes. They protect our public health and safety. They protect our environment. They play a role in our daily lives, and usually in very positive ways.

While discussions of regulatory issues often highlight disagreement among us, I believe everyone generally agrees that some regulation is necessary and good. Our job then is to help ensure the regulatory process is working, with a focus not just on reducing burdens, but also on ensuring transparency and efficiency. And we need to do this while achieving the greatest public benefit.

While there are certainly things about the regulatory process that can be improved, disagreements about the content of a particular rule don't necessarily mean the process isn't working. The process we have in place today gives businesses, individual citizens, and really anyone interested in participating in the process the opportunity to do so. Agencies are required to take their input into account. But as we all know, that doesn't mean everyone will be happy with the final product.

Over the past year, Chairman Johnson has made a number of inquiries related to several of the Administration's rulemakings, including the Department of Labor's Fiduciary Rule, the Environmental Protection Agency's Waters of the United States Rule, and the Federal Communications Commission's Open Internet Rule. As Ranking Member of this Committee, I directed my staff to participate in these inquiries. After reviewing the information we received, we found that the process the Administration used to develop these rules was careful and deliberative.

One example is the Department of Labor's Fiduciary Rule, which requires financial advisers to act in their clients' best interest when they give retirement investment advice. The rule is designed to address conflicts of interest in the industry that encourage some bad actors to push their customers into financial products that may generate higher fees and lower returns. My staff

found that the Department of Labor engaged in an extensive effort to solicit input from the public when developing the rule, including by receiving and reviewing hundreds of hours of testimony and thousands of comments. The Department also sought input from other agencies, which included high-level engagement between Secretary of Labor Tom Perez and Securities and Exchange Commission Chair Mary Jo White. As a result of these consultations, the Department of Labor was able to incorporate changes and improve the rule before it was finalized.

Another example is the Environmental Protection Agency's Waters of the United States Rule, which clarifies the wetlands and streams that must be protected under the Clean Water Act and seeks to maintain safe quality standards in our rivers, bays, and coastal waters. The process the Environmental Protection Agency used to finalize this rule was not hasty, and in fact involved a public comment that was held open for more than 200 days and attracted more than one million comments. In addition, the EPA and Army Corps of Engineers held more than 400 meetings with stakeholders across the country and visited farms in nine states. All of this helped to shape the final rule for the better.

Finally, the Federal Communications Commission also conducted a robust process to solicit input for its Open Internet Rule. Over a five month comment period, the Commission received approximately 3.7 million comments, which is the highest number of comments received on any rulemaking in the agency's history.

I understand not everyone will agree with these three rules the committee is examining today. But I think we can take comfort in knowing the process to develop them was thorough and thoughtful. Since these rules have only been recently finalized, I plan to continue monitoring them closely to ensure they are implemented well. After participating in Chairman Johnson's inquiry, my staff prepared a set of materials, including a memorandum summarizing our findings on the Fiduciary Rule. Mr. Chairman, I ask for unanimous consent that these materials be placed in the hearing record.

Thank you, again, Mr. Chairman, for holding this hearing.



Senate Committee on Homeland Security and Governmental Affairs  
“The Administrative State: An Examination of Federal Rulemaking”  
April 20, 2016  
Statement for the Record

Senator Ben Sasse

As prepared for delivery:

Chairman Johnson and Ranking Member Carper, thank you for holding this important hearing.

Government 101 teaches that the federal government has three branches. Congress, the legislative branch, writes the laws, the Executive Branch implements those laws, and the Courts decide cases and controversies in our nation. Unfortunately, this does not consider the powerful “fourth branch” of the federal government – the Administrative State. This powerful branch passes regulations and rules on a daily basis that carry with them the force of law without being held appropriately accountable to the people.

One shocking Competitive Enterprise Institute study documented that 2015 was the record year for the number of pages published in the Federal Register – 82,036. To put this in perspective, federal agencies passed more pages of federal regulations in 2015 than the number of pages of the entire United States tax code.

Unnecessary government regulations create a real regulatory burden on average Americans. For example, the Nebraska Homebuilders Association has explained to me that government regulations account for nearly 25% of the costs associated with the price of a single-family home. There are countless stories from Nebraskans who tell me that complying with burdensome regulations is costly, complex, and unnecessary.

This growth of the Administrative state, and Congress’ complicity in its growth, is not just undesirable or a costly burden; it is fundamentally dangerous for America and its future.

Government officials are always tempted to amass more power for themselves. So our Founders devised a constitutional system with three separate branches to provide specific limits on the federal government through checks and balances.

Article I of the Constitution gives Congress the authority to write our nation's laws, and Article II requires the President to enforce these laws, not unilaterally re-write, ignore, or create new laws.

This hearing is timely held as the U.S. Supreme Court even this week heard oral arguments to determine whether the Obama Administration’s executive actions regarding deferred action are in accordance with the rule of law and the President’s duty to “take care” to enforce the laws.

Regarding these executive actions, President Obama told Univision in 2014, “I am President. I am not a king...I can’t do these things just by myself. We have a system of government that requires Congress to work with the executive branch to make it happen.”

Yet President Obama and his executive branch has done the opposite.

Today, this hearing will center on three specific examples of executive overreach – the EPA’s “waters of the United States” (WOTUS) rule, the Department of Labor’s Fiduciary Rule, and the FCC’s net neutrality rule.

The WOTUS rule is a dramatic expansion of EPA’s regulatory power beyond the authority granted to it by Congress in the Clean Water Act. This expansion will have a substantial economic impact on numerous industries including farmers, ranchers, construction companies, conservation workers, as well as state, county, and city authorities. Unelected EPA bureaucrats finalized this rule after receiving nearly a million public comments on the rule, which included opposition from 34 out of 50 states.

The costs and regulations associated with the Department of Labor’s Fiduciary Rule may lead investment advisors to stop providing middle class families with the investment advice they want and need. The rule springs from the disdainful belief apparently held by federal bureaucrats/Administration officials that Americans cannot make decisions about whether to pay someone for financial advice or when to trust that advice, and ultimately that they, the Washington D.C. central planners, can make better choices for Nebraskans than we can.

The Net Neutrality rule is a unilateral power grab by the FCC over the internet using the authority from an 80-year-old telecommunications law that was passed long before the internet existed. FCC Commissioner Ajit Pai noted that the rule “gives the FCC the power to micromanage virtually every aspect of how the internet works. It’s an overreach that will let Washington bureaucracy, and not the American people, decide the future of the online world.”

I oppose all three executive branch rules not only because of their enormous economic impact on Americans, but also because they are each a dramatic expansion of federal regulatory authority without the consent of Congress.

The United States is in the midst of a constitutional crisis with an executive branch that has consistently circumvented the Constitution’s limits by acting unilaterally. Nebraskans want a Congress and Executive Branch that respect the rule of law and the Constitution. If members of Congress pass bad laws, voters get to fire them. But when unelected bureaucrats ignore or unilaterally rewrite laws, voters are disenfranchised and lose confidence in the American Experiment.

I will continue to work with my colleagues to address these vital concerns. Congress must reclaim her Article I powers and hold this administration and future administrations – both Republican and Democrat – accountable to the principles enshrined in our nation’s founding documents.

**Written Statement**

**Jonathan Turley,  
Shapiro Professor of Public Interest Law  
The George Washington University Law School**

*“The Administrative State: An Examination of Federal Rulemaking”*

**Dirksen Senate Office Building  
United States Senate**

April 20, 2016

**I. INTRODUCTION**

Chairman Johnson, Ranking Member Carper, and members of the Committee, my name is Jonathan Turley and I am a law professor at George Washington University where I hold the J.B. and Maurice C. Shapiro Chair of Public Interest Law. It is an honor to appear before you today to discuss the rise of the Administrative State within the American constitutional system.

I have long written about the rise of a “fourth branch” in our system and, while academics have good-faith disagreements over the implications of this trend, I believe that this rise of an Administrative State is neither benign nor inevitable. By dismissing the rising power of federal agencies as irreversible and inevitable, many academics portray the changes in our constitutional system as a *fait accompli*—a reality as fixed as the weather in our system. Conversely, critics are often portrayed as quixotic figures tilting at the windmills of federal agencies. There is a false association with the natural growth of the size of government and the emergence of an Administrative State. Clearly, the government has necessarily grown with the increasing size of our population and governmental function. That does not mean, however, that federal agencies must inevitably possess the type of insulated, independent power that they wield today. No one is seriously questioning the need for federal agencies and no one should deny the myriad of important and beneficial actions that agencies take in supporting our security, public health, economy, and environment. Citing the need for federal agencies therefore is hardly an answer to the criticism of the Administrative State—no more than recognizing the need for banks is an answer to a criticism of banking abuses. The fundamental issue raised in hearings like this is how to maintain a large system of federal agencies and offices, without altering the foundation of our constitutional system—particularly our system of separation of powers.

The unavoidable fact is that our system is changing in a fundamental way without a serious debate over the shifting of the center of governmental authority from the legislative process to an administrative process.<sup>1</sup> Indeed, the term “rulemaking” is

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<sup>1</sup> This growth of agency power and independence is occurring at a time of greater unilateral executive power. The rise of the Administrative State combined with both the

something of a misnomer in suggesting that agencies create rules that simply implement the mandates set by the legislative and executive branches. These rules have every characteristic of legislation, indeed frequently involving sweeping changes that impact large parts of our economy.<sup>2</sup> As Chief Justice John Roberts noted recently, rulemaking is in all practical respects an exercise of legislative rather than executive powers.<sup>3</sup> While the Court continues to maintain that Congress cannot delegate legislative powers to agencies, the rhetoric behind decisions like *Whitman v. American Trucking Assn.* is difficult to square with reality.<sup>4</sup> Rulemaking has become a virtual euphemism for agency legislation: the substitution of the Administrative Procedure Act (APA) for the constitutional legislative process. That shift has taken a system designed to guarantee an open process of representative democracy and removed it to an opaque process of administrative decision-making. While some academics may believe that modern government demands the type of ministry system found in Europe, the APA was never intended to be the framework for a new bureaucratic government to replace representative democratic government. The APA was not created to achieve the transformative political process embodied in the tripartite system. Likewise, the Framers did not create a carefully balanced tripartite system with the understanding that the system could be made discretionary with the emergence of an agency alternative to resolve social, political, and economic questions. Most importantly, the public has been given little voice in the emergence of the Administrative State. They are little more than the subject—rather than the source—of the power exercised by federal agencies. My fear is that while there is still time to reverse this trend, we are fast approaching the constitutional fail-safe line where the Administrative State will become a fixed and unassailable reality of American government.

What is fascinating to me is how the rise of the Administrative State has secured what the Framers sought to deny—a new type of “royal prerogative.” The Framers divided the powers of government against the backdrop of over 150 years of tension with the English monarchy.<sup>5</sup> They were specifically aware of the circumvention of the legislative and judicial branches by sovereigns like James I. The King insisted that the enactment of laws was merely the starting point of legislation and that he himself—not just legislators or judges—played a critical role in perfecting laws. He insisted that “I

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rise of an “uber presidency” and the decline of congressional power is a perfect storm for our constitutional system. See generally Jonathan Turley, *A Fox in the Hedges: Vermeule’s Vision of Optimized Constitutionalism in a Suboptimal World*, 82 U. CHI. L. REV. 517 (2015).

<sup>2</sup> See Gary Lawson, *Federal Administrative Law*, (6th ed. 2013) (“When an agency engages in rulemaking, it does something that looks very much like a legislature passing a law.”).

<sup>3</sup> *City of Arlington v. FCC*, 133 S. Ct. 1863, 1877 (2013) (Roberts, C.J., dissenting) (“as a practical matter . . . exercise legislative power, by promulgating regulations with the force of law.”).

<sup>4</sup> 531 U.S. 457, 487-90 (2001).

<sup>5</sup> See Julius Goebel, Jr., *Ex Parte Clio*, 54 COLUM. L. REV. 450, 474 (1954); David Gray Adler, *The Steel Seizure Case And Inherent Presidential Power*, 19 CONST. COMMENT. 155, 164 (2002).

thought law was founded upon reason, and I and others have reason as well as the judges.”<sup>6</sup> That was precisely the view rejected by the Framers. Thomas Jefferson wrote in 1783 with regard to the Virginia Constitution that “[b]y Executive powers, we mean no reference to the powers exercised under our former government by the Crown as of its prerogative . . . We give them these powers only, which are necessary to execute the laws (and administer the government).”<sup>7</sup> Likewise, James Wilson defended the model of an American president by assuring his colleagues that he “did not consider the Prerogatives of the British Monarch as a proper guide in defining the Executive powers. Some of these prerogatives were of a Legislative nature.”<sup>8</sup> While the Framers opposed this role in crafting the first three articles of the Constitution, a type of “agency prerogative” has arisen within the system that is founded on the very same premise articulated by James I. As with the use of unilateral executive power, agency decisions now claim to further the legislative process through administrative reasoning. Legislation is treated as merely the starting point of legislation with agencies “perfecting” the law through rulemaking. This prerogative is protected from meaningful judicial review by the *Chevron* doctrine and the administrative procedural system. In the last few years, we have seen such agency actions achieving the very legislative changes that the Administration failed to secure in Congress. Where the denial of such legislation was once considered the end of the matter, a failure in Congress is now treated as a prelude to seeking the same results by the alternative means of agency action. When signed by a president, congressional enactments were meant to be the completion, not the initiation, of the process of legislation.

Congress still possesses the authority to reclaim its defining role over the legislative process. As discussed below, Congress can move to counter claims of delegated authority and even limit the degree of deference afforded agency decision-making. If Congress is to rebalance the system, however, it will need to enhance its staff and enlist the public in checking agency authority. This does not mean the end of rulemaking or the elimination of federal agencies. Likewise, no one is suggesting the micromanagement of federal agencies, but rather the placement of checks on agencies to guarantee that the term “Administrative State” remains a warning rather than a reality in our system.

## II. THE RISE OF A FOURTH BRANCH IN A TRIPARTITE SYSTEM.

I have previously written<sup>9</sup> and testified<sup>10</sup> about the rise of the Fourth Branch and

<sup>6</sup> 7 Sir Edward Coke, Reports 65, quoted in ROSCOE POUND, THE SPIRIT OF THE COMMON LAW 61 (1921).

<sup>7</sup> This quote is from Jefferson’s Draft of a Fundamental Constitution for Virginia. Adler, *supra* note 5, at 164 (citing CHARLES WARREN, THE MAKING OF THE CONSTITUTION 177 (Harvard U. Press, 1947)).

<sup>8</sup> THE RECORDS OF THE FEDERAL CONVENTION OF 1787 at 62-70 (Max Farrand, ed 1911); Adler, *supra* note 5, at 165.

<sup>9</sup> See, e.g., Jonathan Turley, *Madisonian Tectonics: How Form Follows Function in Constitutional and Architectural Interpretation*, 83 GEO. WASH. L. REV. 305 (2015); Jonathan Turley, *A Fox in the Hedges: Vermeule’s Vision of Optimized Constitutionalism*

the growing imbalance in our governmental system. The American governmental system has obviously changed dramatically since the founding, when the vast majority of governmental decisions rested with state governments. In 1790, the federal government was smaller than most modern city governments, employing only about one thousand nonmilitary workers. By 1962, that number had grown to 2,515,000 federal employees. Notably the first regulatory federal agency, the Interstate Commerce Commission, was not established until 1887.<sup>11</sup> The rise of the Administrative State is generally traced to the New Deal; though its roots preceded the Great Depression, there was a clear shift in the view of government. Before the New Deal, the government was often viewed as a necessary evil: a centralized system that overcame the problems of the Articles of Confederation, but that also remained an ever-present threat to individual liberty. With the onset of the Great Depression, the government was seen as the transformative institution to rescue the public from economic and public health threats. The academic literature also shifted during this period. Frankly, academics have a certain affinity for agency experts who share educational backgrounds as well as a common commitment to public policy. Conversely, there is little identification with Congress, which academics

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in a Suboptimal World, 82 U. CHI. L. REV. 517 (2015); Jonathan Turley, *Recess Appointments in the Age of Regulation*, 93 B.U. L. REV. 1523 (2013); Jonathan Turley, *The Rise of the Fourth Branch of Government*, WASH. POST (May 24, 2013); see also Jonathan Turley, *Constitutional Adverse Possession: Recess Appointments and the Role of Historical Practice in Constitutional Interpretation*, 2013 WIS. L. REV. 965 (2013) (discussing the separation of powers consequences in the reduction of legislative authority).

<sup>10</sup> See “*The Chevron Doctrine: Constitutional and Statutory Questions in Judicial Deference to Agencies*,” United States House of Representatives, House Judiciary Committee, Regulatory Reform, Commercial and Antitrust Law, March 15, 2016; *Authorization to Initiate Litigation for Actions by the President Inconsistent with His Duties Under the Constitution of the United States: Hearing Before the H. Comm. on Rules*, 113th Cong. (2014) (prepared statement of Jonathan Turley, Shapiro Professor of Public Interest Law, The George Washington University Law School), <http://docs.house.gov/meetings/RU/RU00/20140716/102507/HMTG-113-RU00-Wstate-TurleyJ-20140716.pdf>; *Enforcing The President’s Constitutional Duty to Faithfully Execute the Laws: Hearing Before the H. Comm. on the Judiciary*, 113th Cong. 30–47 (2014) (testimony and prepared statement of Jonathan Turley, Shapiro Professor of Public Interest Law, The George Washington University Law School) (discussing nonenforcement issues and the rise of the Fourth Branch); *Executive Overreach: The President’s Unprecedented “Recess” Appointments: Hearing Before the H. Comm. on the Judiciary*, 112th Cong. 35–57 (2012) (prepared statement of Jonathan Turley, Shapiro Professor of Public Interest Law, The George Washington University Law School); see also *Confirmation Hearing for Attorney General Nominee Loretta Lynch: Hearing Before the S. Comm. on the Judiciary*, 114th Cong. (2015) (prepared statement of Jonathan Turley, Shapiro Professor of Public Interest Law, The George Washington University Law School) (discussing the loss of legislative power and the role of confirmation hearings to address separation of powers issues).

<sup>11</sup> Interstate Commerce Act, ch. 104, 24 Stat. 445 (1887).

view as turning on persuasion rather than proof. Not surprisingly, academic work tends to view agencies as public policy experts equipped to deal with complex issues while dismissing Congress as a body with transient interests and limited expertise in given fields.

The New Deal brought young reformers to Washington with advanced degrees and unlimited optimism for the prospect that massive social problems could be eradicated through government intervention. In many areas, they were largely successful in correcting hazards in the workplace, cleaning up the environment, fighting poverty, and improving education. The role of federal agencies, however, began to change as Congress yielded more and more of its authority to agency decision-making, while courts removed themselves from meaningful review through the adoption of the *Chevron* doctrine and other rulings. The greatest barrier to this shift was the Separation of Powers doctrine. When Franklin Roosevelt proclaimed, “The day of enlightened administration has come,”<sup>12</sup> it represented the end of the day for the traditional or formalist view of the Separation of Powers. It was not simply the creation and expansion of federal agencies, but rather their increasingly *independent* role. Agencies sought “enlightened” approaches to social problems based on scientific and policy expertise while Congress was increasingly viewed as uninformed, untrained, and unreliable in dealing with such issues with any degree of specificity. Strangely, it was a view that many in Congress seemed to accept or at least yield to over the course of time.

As the scope and complexity of federal programs increased, Congress relinquished more and more authority over those programs. As discussed below, this trend led to the virtual evisceration of the “nondelegation doctrine”—the constitutional requirement that Congress cannot delegate its legislative authority to federal agencies. Active congressional control over agency actions became viewed as virtually anachronistic in the “Age of Regulation.” Federal agencies—and many in the public and academia—viewed Congress as a choke point. Given the size of the federal government, the relatively small staff of Congress could do little to monitor, let alone direct, federal agencies. We now have roughly 2,840,000 federal workers in 15 departments, 69 agencies, and 383 nonmilitary sub-agencies.<sup>13</sup> This does not count the millions of contractors and subcontractors working for the government. These federal offices and workers largely follow rules that arose organically within the agency. The agencies now have the elements of microcosmic government systems in and of themselves. They even hold town halls to measure public sentiment and explain their actions to citizens. Thus,

<sup>12</sup> Franklin D. Roosevelt, Campaign Address on Progressive Government at the Commonwealth Club, San Francisco, Cal. (Sept. 23, 1932), in 1 THE PUBLIC PAPERS AND ADDRESSES OF FRANKLIN D. ROOSEVELT, THE GENESIS OF THE NEW DEAL, 1928-32, at 752 (1938).

<sup>13</sup> Turley, *Recess Appointments in the Age of Regulation*, *supra* note 9, at 1533; WALTER E. VOLKOMER, AMERICAN GOVERNMENT 231 (11th ed. 2006) (citing Bruce D. Porter, *Parkinson’s Law Revisited: War and the Growth of American Government*, 60 PUB. INT. 50, 50 (1980)). In 1816, the federal system employed 4,837 employees. Deanna Malatesta, *Evolution of the Federal Bureaucracy*, in 1 A HISTORY OF THE U.S. POLITICAL SYSTEM: IDEAS, INTERESTS, AND INSTITUTIONS 373, 380 tbl.1 (Richard A. Harris & Daniel J. Tichenor eds., 2010).

the term “fourth branch” itself may itself be something of a misnomer. The agencies do not truly operate in concert. Rather they represent insular and largely self-contained government systems—much like administrative versions of feudal estates. There is no true center to the current system with its thousands of independently moving parts and agendas. While the White House clearly can dictate changes or priorities (as it recently did in areas like health care and immigration), most rulemaking changes arise organically within these agencies. Absent a relatively rare intervention from Congress, these changes are largely crafted, debated, and promulgated within agency systems.

### III. AGENCY LEGISLATION AND THE ADMINISTRATIVE STATE

The growth in the size of the federal government resulted in a shift in the center of gravity for the system as a whole. Massive federal agencies now promulgate regulations, adjudicate disputes, and apply rules in a system that affords relatively little transparency or accountability to the public. While subject to congressional review in theory, the reality is that Congress has relatively few staff members and little time for such reviews. As a result, it is the Administrative State, not Congress, that now functions as the dominant “law giver” in our system. The vast majority of “laws” governing the United States are not passed by Congress but are issued as regulations, crafted largely by thousands of unseen bureaucrats. For example, in 2007, Congress enacted 138 public laws, while federal agencies finalized 2,926 rules, including 61 major regulations.<sup>14</sup> Agencies now adjudicate most of the legal disputes in the federal system. A citizen is ten times more likely to be tried by an agency than by an actual court. In a given year, federal judges conduct roughly 95,000 adjudicatory proceedings, including trials, while federal agencies complete more than 939,000. This is not to imply that such regulations and adjudications are inherently tyrannical or that Congress has no influence over agencies. Rather, it states the obvious: this system is adopting new pathways and power centers that were never anticipated in the design of our system.

The nondelegation doctrine is based on the notion that our carefully balanced system of government cannot fully function if the legislative process left to Congress in the vesting clause (including such guarantees as presentment and bicameralism) can simply be circumvented. U.S. Const. art. I, §1 (“All legislative Powers herein granted shall be vested in a Congress of the United States . . .”). While the Supreme Court has long reaffirmed the need for Congress to exercise such powers, it created a fluid test that allowed agencies to “fill up the details” left by legislation in the execution of laws.<sup>15</sup> The Court allowed delegation of rulemaking powers if there is an “intelligible principle”<sup>16</sup>: a standard that has proven perfectly unintelligible in allowing any statutory reference—short of utter silence<sup>17</sup>—to suffice for delegation. This reality was expressly

<sup>14</sup> Anne Joseph O’Connell, *Vacant Offices: Delays in Staffing Top Agency Positions*, 82 S. CAL. L. REV. 913, 936 (2009).

<sup>15</sup> *United States v. Shreveport Grain & Elevator Co.*, 287 U.S. 77, 85 (1932).

<sup>16</sup> *Loving v. United States*, 517 U.S. 748, 772 (1996).

<sup>17</sup> *Yakus v. United States*, 321 U.S. 414, 426 (1944) (“Only if ... there is an absence of standards ... would we be justified in overriding [the congressional] choice of means for effecting its declared purpose.”).



acknowledged in the Court's decision in *Whitman v. American Trucking Ass'n*.<sup>18</sup> In that case, the Court noted "we have found the requisite 'intelligible principle' lacking in only two statutes, one of which provided literally no guidance for the exercise of discretion, and the other of which conferred authority to regulate the entire economy on the basis of no more precise a standard than stimulating the economy by assuring 'fair competition.'" Thus, in *Yakus*, the Court upheld the Emergency Price Control Act (EPCA) when Congress gave to the Office of Price Administration (OPA) the power to set commodity prices that "in his judgment will be generally fair and equitable and will effectuate the purposes of the Act."<sup>19</sup> The Court had flipped the presumption and embraced the idea that Congress could pick the path of least resistance in yielding core legislative responsibilities to bureaucrats. The Court held that Congress "is free to avoid the rigidity of such a system, which might well result in serious hardship, and to choose instead the flexibility attainable by the use of less restrictive standards."<sup>20</sup> That "flexibility" is often driven more by political than policy realities. Given the opportunity to pass highly generalized (indeed even aspirational) bills, Congress can often avoid tough calls and decisions by passing the more difficult substantive policy decisions off to federal agencies. This is precisely what the Framers had sought to avoid in forcing policy disagreements into the legislative process. The transfer of power is more than transferring these problems to bureaucrats; robs the system of its essential role in forcing majoritarian compromise.

Madison believed that the separation of powers, as a structure, could defeat the natural tendency to aggrandize power that tended toward tyranny and oppression. In Madison's view, "the interior structure of the government"<sup>21</sup> distributed the pressures and destabilizing elements of nature in the form of factions<sup>22</sup> and unjust concentration of power.<sup>23</sup> He envisioned what he described as a "compound" rather than a "single" structure republic and suggested it was superior because it could bear the pressures of a large pluralistic state. Alexander Hamilton spoke in the same terms, noting that the superstructure of a tripartite system allowed for the "distribution of power into distinct departments" and for the republican government to function in a stable and optimal fashion.<sup>24</sup>

The structure of this system represents more than just the rigid lines defining inter-branch powers. The structure is meant to transform factional interests into majoritarian compromises. I have previously written about what I call a "conarchitectural" approach

<sup>18</sup> *Whitman v. Am. Trucking Ass'n*, 531 U.S. 457, 474 (2001) (citing *Panama Refining Co. v. Ryan*, 293 U.S. 388 (1935); *A. L. A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935)).

<sup>19</sup> *Id.* at 420.

<sup>20</sup> *Id.* at 425-26.

<sup>21</sup> THE FEDERALIST NO. 51, at 320 (James Madison).

<sup>22</sup> See THE FEDERALIST NO. 10, at 79 (James Madison) (noting that the "causes of faction" are "sown in the nature of man.").

<sup>23</sup> See THE FEDERALIST NO. 51, *supra* note 21, at 320 (James Madison); see also Douglass Adair, "That Politics May Be Reduced to a Science": David Hume, James Madison, and the Tenth Federalist, 20 HUNTINGTON LIBR. Q. 343, 348-57 (1957).

<sup>24</sup> THE FEDERALIST NO. 9, at 72 (Alexander Hamilton).

to constitutional interpretation and understanding the separation of powers.<sup>25</sup> In architecture, the concept of structure has been developed to a far greater extent than in the law, despite our long-standing debate of form and functionalism. It is well understood that structure does not just protect those within but also directs their interrelationships. As Winston Churchill once said, “[t]here is no doubt whatever about the influence of architecture and structure upon human character and action. We make our buildings and afterwards they make us.”<sup>26</sup> The design of the structure both reflects and directs the action within it. In both architectural and constitutional theory, form follows function. The separation of powers forces a greater array of participating actors, and therefore interests, to be considered in the shaping of laws. A conarchitectural approach treats the structure itself as the expression of the Framers’ vision of human nature and the optimal space for political deliberations.<sup>27</sup>

As in architecture, constitutional structure plays a determinist role in shaping perspective and choice. The structural lines and spaces created by the Framers are best seen as a recognition of the need to frame not just the inherent powers but the perception of power within a system. By structuring political decision-making, constitutional structure funnels both the decision-making and political dialogue along particular pathways. The confines of the tripartite system serve much of the same function as “choice architecture” in funneling political energies and actions. By maintaining separation, the Framers likely sought to achieve stability even within the dynamic and divisive political environment. The guarantees of separation ideally discouraged dysfunctional choices that Congress or a President might make in an effort to circumvent one another or “go it alone” through unilateral action.<sup>28</sup> The structure was not only shaped by human realities, but would, in turn, even help shape those realities. The limitations on executive, legislative, and judicial powers were meant to limit the horizons of power; to influence the range of choices and expectations within the system. When viewed from this perspective, the rise of a system of federal agencies within the constitutional structure changed how those within it interact and react. The tripartite design of the Madisonian system is carefully calculated to resolve divisions in a pluralistic society.

Social and political divisions were never meant to be resolved through an array of federal agencies, which are insulated from the type of public participation and pressures that apply to the legislative branch. A recent example is the intervention of a small federal office to force a result in the long-simmering public debate over the name of the

<sup>25</sup> See, e.g., Turley, *Madisonian Tectonics*, *supra* note 9; Jonathan Turley, *A Fox in the Hedges*, *supra* note 9.

<sup>26</sup> Paul Goldberger, *Why Architecture Matters* 1 (Yale 2009) (quoting Churchill’s address to the English Architectural Association in 1924).

<sup>27</sup> This notion of constitutional structure can present classic “soft variable” issues for theories incorporating economic or risk elements into the analysis. See generally Turley, *A Fox in the Hedges*, *supra* note 9.

<sup>28</sup> The controversy over the nonenforcement of federal law is a direct result of “bad choices” made in the absence of clear lines of separation as I have previously discussed before Congress. See *Duty to Faithfully Execute Hearing*, *supra* note 10, at 113–63; see also Jonathan Turley, *The President’s Power Grab*, L.A. TIMES, Mar. 9, 2014, at A28.

Washington Redskins football team.<sup>29</sup> The Trademark Trial and Appeal Board voted to rescind federal trademark protections for the Redskins—a decision that could ultimately decide the controversy over the 80-year-old name. There are perfectly good reasons to be offended by this name, but the public remains deeply divided. Social and market pressures may still result in a name change but it should not come by some administrative edict of the little-known administrative body of a little-known board. The problem is that the board had at its disposal a ridiculously ambiguous standard which allows the denial of a trademark if it “may disparage” a “substantial composite” of a group at the time the trademark is registered. Congress should have addressed that ill-defined standard years ago, but the overreach of the board was breathtaking. We have seen other examples of agencies intervening in political or social controversies in ways that undermine the legislative process as the means for resolving such conflicts, as I have previously discussed.<sup>30</sup>

While the future of the Redskins name is hardly a threat to our system of government, the circumvention of political process in such controversies is such a threat. We are gravitating toward the de facto creation of an English ministry system. Academics often treat the rise (and dominance) of the Administrative State as an inevitability and, accordingly, view those of us who cling to the Madisonian model as hopelessly naïve and nostalgic. Until the American people decide to adopt a bureaucracy or technocracy as the principle form of government, however, Congress has a duty to act to preserve the essential components of our tripartite system. To do that, it must first deal with *Chevron*.

### III. RESTORING THE TRIPARTITE SYSTEM THROUGH THE RECLAMATION OF LEGISLATIVE AUTHORITY.

What is particularly striking is how many academics treat the Administrative State as now an obvious and irreversible part of our constitutional system. Indeed, when I recently testified on the *Chevron* doctrine, I was struck by the critique of one of my colleagues of changes to the deference afforded to agencies as inimical to the Administrative State. It now seems that the Administrative State is so part of our governing system that it must be sustained like a symbiotic growth that is now essential to sustain the life of the host. While it is true that we practically cannot function without agencies, it is also true that agencies can function without sweeping deference or delegation. Yet, our system is fast approaching a point where this shift will become irreversible. Legislative authority is at its lowest point in the history of our Republic. If agencies are allowed to continue to solidify governing authority, our system will gradually lose any real functional meaning as a representative democracy (as opposed to a government run by EU-like directorates or ministries). This may be (in the view of some academics) a better system, but it is not the system that citizens of this country accepted and any departure from that original model should be left to the citizens who will have to live under the new model.

<sup>29</sup> Jonathan Turley, *Another Federal Agency Goes Outside of Bounds Over Redskins Name*, WASH. POST (Sunday), June 22, 2014.

<sup>30</sup> Jonathan Turley, *Politics by Other Means*, USA TODAY, July 8, 2014.

A. *Returning To The Pre-Chevron Model Of The APA.*

The good news is that the Administrative State is a creation—by both congressional action and acquiescence—of Congress. What Congress created, Congress can remake. As the Supreme Court has made clear, “Agencies are creatures of Congress; ‘an agency literally has no power to act . . . unless and until Congress confers power upon it.’”<sup>31</sup> Accordingly, this is an area where Congress can have a direct and pronounced impact. The question is not the authority but the desire of Congress to reassert its authority over agencies. Indeed, had Congress remained faithful to the original vision of the Administrative system (and had courts not removed themselves from this area through cases like *Chevron*), we would not be witnessing this unprecedented shift of governing authority to agencies. Congress expressly created a system of review to constrain agency abuses. Section 706(2) of the Administrative Procedure Act (APA) states that courts shall:

hold unlawful and set aside agency action, findings, and conclusions found to be –

- (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;
- (B) contrary to constitutional right, power, privilege, or immunity;
- (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right;
- (D) without observance of procedure required by law . . . .

The statutory duty to decide whether an agency action is “in excess of statutory jurisdiction, authority, or limitations, or short of statutory right” reflects a traditional judicial review standard. There is no license for yielding a substantial part of that duty to agencies as presumptively correct interpreters of the law. In the APA, Congress specifically instructed courts to decide “all relevant questions of law.”<sup>32</sup> When read in combination with the APA, *Chevron* reads as much a delegation of judicial function as legislative function.

*Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*<sup>33</sup> addressed the question of how the Environmental Protection Agency (EPA) could treat “non-attainment” states that had failed to attain the air quality standards under the Clean Air Act. The Reagan Administration had liberalized preexisting rules requiring a permit for new or modified major stationary sources. The Natural Resources Defense Council challenged the EPA regulation and prevailed in court. With three justices not participating in the decision, the court voted 6-0 to reverse and order deference to the EPA’s interpretation.<sup>34</sup>

<sup>31</sup> *City of Arlington*, 133 S. Ct. at 1880 (quoting *Louisiana Pub. Serv. Comm’n v. FCC*, 476 U. S. 355, 374 (1986)).

<sup>32</sup> 5 U.S.C. § 706 (2016).

<sup>33</sup> *Chevron*, 467 U.S. 837 (1984).

<sup>34</sup> Chief Justice Rehnquist, Justice Thurgood Marshall, and Justice Sandra Day O’Connor recused themselves from the case.

The *Chevron* decision proved to be something of a Trojan horse doctrine that arrived in a benign form but soon took on a more aggressive, if not menacing, character for those concerned about the separation of powers. On its face, the doctrine is unremarkable and even commendable in a Court seeking to limit the ability of unelected judges to make arguably political decisions over governmental policy. As noted by Chief Justice John Roberts, “*Chevron* importantly guards against the Judiciary arrogating to itself policymaking properly left, under the separation of powers, to the Executive.”<sup>35</sup> *Chevron* put forward a simple test for courts in first looking at whether the underlying statute clearly answers the question and, if not, whether the agency’s decision is “permissible” or reasonable.<sup>36</sup> That highly permissive standard shifted the center of gravity of statutory interpretation from the courts to the agencies, contrary to the language of the APA. With sweeping deferential language, the Court practically insulated agencies from meaningful review. In a system based on checks and balances, the Court helped create an internal system that would flourish under a protective layer of agency deference. To be sure, the Court has repeatedly recognized the right of Congress to check federal agencies. In practice, however, *Chevron* has proven a windfall for agencies, advancing their priorities and policies in the execution of federal laws. It is the administrative equivalent of *Marbury v. Madison*. Rather than declaring courts as the final arbiter of what the law means in *Marbury*, *Chevron* practically resulted in the same thing for agencies, giving them the effective final word over most administrative matters. Even though Congress can override agency decisions, it is unrealistic to expect millions of insular corrections to be ordered over agencies decisions.

Before *Chevron*, there was not a period of utter confusion and judicial tyranny in the review of agency decisions. Courts simply applied traditional interpretive approaches that looked at whether there was an ambiguity or gap in a statute as opposed to clarity on a given question. If so, it then reviewed the agency decision to determine whether it was legal and proper. This analysis was later developed further by the decision in *Skidmore v. Swift & Co.*, where the Court articulated factors used to decide whether to overturn the particular agency’s determinations.<sup>37</sup> Notably, without granting sweeping deference, the Court in *Skidmore* already recognized that agency determinations would carry weight, just not controlling weight:

We consider that the rulings, interpretations and opinions of the Administrator under this Act, while not controlling upon the courts by reason of their authority, do constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance. The weight of such a judgment in a particular case will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control.

*Id.* Justice Jackson referred to a historical treatment of agency interpretations with due

<sup>35</sup> *City of Arlington v. FCC*, 133 S. Ct. 1863, 1886 (2013) (Roberts, C.J., dissenting).

<sup>36</sup> *Chevron*, 467 U.S. at 842-43.

<sup>37</sup> *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944).

“respect” and “considerable weight.” *Id.* at 140. Thus, the courts did not have a hostile or counter-agency position in such cases, but a fairly accommodating standard. Courts in the United States also have a well-understood and respected tradition of avoiding political questions and limiting judicial discretion. *Chevron* could have resulted in the very same way under this prior case law, but the Court instead created a new deferential standard that proceeded to expand as soon as the Court gave it breath.

After decades of neglect during which the Court remained relatively passive in the face of the rising dominance of agencies in our system, the Court began to seek incremental limitations on the authority of agencies. While Justice Scalia called *Skidmore* “an anachronism”<sup>38</sup> the Court would rediscover the value of more serious judicial review in other cases. For example, in *Christensen v. Harris County*,<sup>39</sup> the Court suggested that the prior standard in *Skidmore* would apply to less formal agency decisions as opposed to those agency documents that carry “force of law.” Justice Clarence Thomas drew a distinction of when an agency interprets a statute in a decision that has “the force of law” from more rudimentary decision. As noted by Professor Thomas Merrill,<sup>40</sup> Thomas’ proposal tracked a recommendation by the Administrative Conference of the United States.<sup>41</sup> Thomas described the former category as including “formal adjudication or notice-and-comment rulemaking.”<sup>42</sup> Thus, because this case involved a Department of Labor opinion letter that was merely advisory on the meaning of the Fair Labor Standards Act, there was no deference extended under *Chevron*. In applying the *Skidmore* standard, the Court rejected the interpretation. Differing minority opinions added to the confusion of the current meaning of *Chevron*, including the dissenting opinion of Justice Breyer, who insisted that *Chevron* did not create a new standard, and that *Skidmore* remains the only standard for deference.<sup>43</sup> *Chevron*, in his view, only extended the basis for deference on the basis that “Congress had delegated to the agency the legal authority to make those determinations.”<sup>44</sup>

The evolving and conflicting view of *Chevron* was also captured in the decision of *United States v. Mead Corp.*<sup>45</sup> In that case of tariff classification rulings, the eight-justice majority opinion, recognized different deference tests under *Skidmore* and *Chevron*. Consistent with *Christensen*, the Court noted the application of *Chevron* for agency interpretations that have the “force of law.”<sup>46</sup> The Court embraced the notion of delegated authority from Congress for “the agency generally to make rules carrying the

<sup>38</sup> *Christensen v. Harris Cty.*, 529 U.S. 576, 589 (2000) (Scalia, J., concurring in part and concurring in the judgment).

<sup>39</sup> *Christensen*, 529 U.S. 576 (2000).

<sup>40</sup> See generally Thomas Merrill, *Chevron at 30: Looking Back and Looking Forward: Step Zero After City of Arlington*, 83 FORDHAM L. REV. 731 (2014).

<sup>41</sup> OFFICE OF THE CHAIRMAN, ADMIN. CONFERENCE OF THE U.S., RECOMMENDATIONS AND REPORTS, RECOMMENDATION 89-5: ACHIEVING JUDICIAL ACCEPTANCE OF AGENCY STATUTORY INTERPRETATIONS 31-33 (1989).

<sup>42</sup> Merrill, *Chevron at 30*, *supra* note 40, at 587.

<sup>43</sup> *Id.* at 596 (Breyer, J., dissenting).

<sup>44</sup> *Id.*

<sup>45</sup> *Mead*, 533 U.S. 218 (2001).

<sup>46</sup> *Id.* at 226-27.

force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority.”<sup>47</sup> However, the condition of what is an action with the force of law remained undefined. Yet, the ruling became the basis for the concept of “Chevron Step Zero,” the courts first inquire into whether Congress delegated the authority before applying *Chevron* deference. If not, the less favorable standard in cases like *Skidmore* would apply.

One of the more alarming applications of *Chevron* came in *City of Arlington v. FCC*.<sup>48</sup> The case concerned a 1996 amendment to the Federal Communications Act mandating that local land use agencies process applications for the construction or modification of wireless transmission towers “within a reasonable period of time.”<sup>49</sup> The statute provided an avenue with a “court of competent jurisdiction” for relief to parties who did not receive action on requests. The case perfectly captured the fluid authority and utter flexibility of agencies in exercising their interpretive powers post-*Chevron*. The Federal Communications Commission (FCC) initially disclaimed the authority under the statute, but then reversed itself and issued an order setting a 90-day limit for any tower expansion or 150-day limit for new construction under the rule. The jurisdictional authority of the FCC was challenged. For many years, it was generally thought that, no matter how expansively *Chevron* was read, the one area where an agency could not claim deference would be in the interpretation of its own jurisdictional powers. After all, as discussed above, the APA specifically leaves to the court to determine if an agency has acted “in excess of statutory jurisdiction.” Nevertheless, the Fifth Circuit held that *Chevron* would apply in an agency defining its own jurisdiction. The Supreme Court agreed in a 5-4 decision with Justice Scalia joining the majority. Chief Justice Roberts (with Justices Kennedy and Alito) dissented. Five Justices found no way to distinguish jurisdictional and non-jurisdictional questions. Indeed, in his separate decision, Justice Scalia called such distinctions little more than a “mirage.”<sup>50</sup>

Chief Justice Roberts, joined by Justices Kennedy and Alito, dissented, and expressed the view that such expanded authority raised transformative challenges for the federal system. Roberts decried the court for evading its core responsibility in drawing lines of authority within that system: “Our duty to police the boundary between the Legislature and the Executive is as critical as our duty to respect that between the Judiciary and the Executive . . . We do not leave it to the agency to decide when it is in charge.”<sup>51</sup> In a chilling warning, Roberts further notes that “[i]t would be a bit much to describe the result as ‘the very definition of tyranny,’ but the danger posed by the growing power of the Administrative State cannot be dismissed.”

*City of Arlington* fulfilled many of our worst fears of the trajectory of *Chevron*. Despite tailoring in cases like *Christensen* and *Mead*, *City of Arlington* gave agencies a

<sup>47</sup> *Id.* at 27.

<sup>48</sup> *City of Arlington v. FCC*, 133 S. Ct. 1863, 1886 (2013).

<sup>49</sup> 47 U.S.C. § 332(c)(7)(B)(ii) (2012).

<sup>50</sup> Justice Scalia saw the distinction as another attack on *Chevron* that would be exploited in future cases. *City of Arlington*, 133 S. Ct. at 1873 (Scalia, J., concurring) (“Make no mistake—the ultimate target here is *Chevron* itself. Savvy challengers of agency action would play the ‘jurisdictional’ card in every case.”)

<sup>51</sup> *Id.* at 1886 (Roberts, C.J., dissenting).

critical and expansive power to define their own jurisdiction under the protection of a heavy *Chevron* deference standard. For that reason, the avoidance of *Chevron* analysis in the recent decision in *King v. Burwell* only deepened the uncertainty over the scope and meaning of the doctrine. The case would seem ripe for *Chevron* analysis in the interpretation of an agency of the meaning of state and federal exchanges within the overall scheme of the Affordable Care Act (ACA). Writing for a six-justice majority, Chief Justice Roberts, wrote:

When analyzing an agency's interpretation of a statute, we often apply the two-step framework announced in *Chevron*. Under that framework, we ask whether the statute is ambiguous and, if so, whether the agency's interpretation is reasonable. This approach is premised on the theory that a statute's ambiguity constitutes an implicit delegation from Congress to the agency to fill in the statutory gaps. In extraordinary cases, however, there may be reason to hesitate before concluding that Congress has intended such an implicit delegation.<sup>52</sup>

It is the type of fluid, undefined standard that has characterized not just the post-*Chevron* cases but many other areas of jurisprudence from the Court. The Court appears to believe that it will be self-evident when a court is dealing with a “question of deep economic and political significance.”<sup>53</sup> Of course, many, if not most, federal agency decisions have significant impacts. While *King v. Burwell* may reflect a degree of belated buyer's remorse, it will hardly correct an ambiguous standard by grafting on an equally ambiguous limitation on that standard. Indeed, the Court appears convinced that adding layers of ambiguity will somehow produce clarity under *Chevron*. Congress can introduce the very clarity that seems to escape the Court by expressly limiting or disavowing delegation in statutes, as discussed below.

#### B. Restoring Legislative Control Over Agency Lawmaking.

If Congress is to reassert its authority over agency lawmaking it will have to develop new pathways for information and limit areas of claimed delegation. The first priority is to reduce the informational costs and barriers for members in monitoring agency actions. I have strongly encouraged Congress to expand legislative staff to allow greater monitoring and correction measures vis-à-vis agency actions. While Congress required independent evaluation by the GAO under the Truth in Regulating Act of 2000,<sup>54</sup> there has not been sufficient funding of this function. Congress should reconsider the establishment of an office that is fully equipped to track and review federal rules and regulations, as proposed under the Strengthening Congressional Oversight of Regulatory Actions for Efficiency Act.<sup>55</sup> The first line of defense for Congress remains its ability to act to check agencies. The very size and complicity of federal regulations, however, make such monitoring sporadic and uncertain without an office with the expertise to

<sup>52</sup> *King v. Burwell*, 135 S. Ct. 2480, 2488-89 (2015) (citations omitted).

<sup>53</sup> *Id.* at 2489.

<sup>54</sup> Pub. L. No. 106-312, 114 Stat. 1248-50 (2000).

<sup>55</sup> S. 1472, 113th Cong. (2013).



facilitate this function. Notably, the Office of Management and Budget (OMB) has a budget of roughly \$100 million annually and a staff of hundreds to monitor executive agencies and programs. The OMB is supported by thousands of agency employees who feed it information on new rulemaking as well as carry out directives on such programs. In comparison, the branch tasked with actually creating and changing the laws under which these agencies operate remains understaffed and overwhelmed. There is no way to do this on the cheap. Either Congress will maintain a staff capable of meaningful monitoring of rulemaking or it will retain a largely pedestrian role with regard to the Administrative State. Obviously, Committee staff serves as the eyes of Congress in different areas of the law. However, those staff members are tasked with other duties from drafting laws to holding hearings to addressing budgets. What is needed is a specialized staff within the legislative branch who can reassert congressional authority over agency law-making.

Congress also needs to create new pathways for checking rulemaking. It has tried to do so in the past with little success. The Congressional Review Act (CRA)<sup>56</sup> allowed Congress to block significant regulations. Yet, both houses had to pass resolutions of disapproval and the president had to sign the law. Not surprisingly, the law had little impact. Another compelling approach would be to classify rulemaking to focus enhanced procedures on the most impactful and substantial forms of rulemaking. That was the case with the proposed amending of the APA with the Regulatory Accountability Act (RAA).<sup>57</sup> Classifying regulations into three categories, “high impact” rules (with estimated effects of \$1 billion or more in a year) would be subject to greater scrutiny and public proceedings. The creation of such formal procedures can not only create greater transparency, but (as discussed below) enlist the public and outside groups in evaluating agency rulemaking.

The current notice and comment provisions under the APA are often criticized as largely cosmetic for agencies, which have already set upon an intended course. While creating highly limited procedural rights and the appearance of participatory systems, agencies have to do relatively little in considering such views before promulgating final rules. Moreover, the process of administrative lawmaking is intransparent except for the perfunctory public comment period. Before and after such notice and comment, agencies are allowed to engage in ex parte communications in the crafting of their policies and programs. As Justice Kagan noted during her academic career, most of the agency deliberations are carried out without a record or public review.<sup>58</sup>

As shown in the current immigration case heard this week by the Supreme Court, the government can implement sweeping changes even without such notice and comment. *United States v. Texas* is a chilling example of how agencies today operate independently from both Congress and the public in dictating changes affecting our society and economy in fundamental ways. While the APA’s notice-and-comment requirements set forth at 5 U.S.C. § 553(b) have been repeatedly enforced by the courts as a precondition

<sup>56</sup> 5 U.S.C. § 801, et seq.

<sup>57</sup> S. 1029, 113th Cong. (2013); H.R. 2122, 113th Cong. (2013).

<sup>58</sup> Elena Kagan, *Presidential Administration*, 114 HARV. L. REV. 2245, 2280 n.142 (2001) (noting that “[t]he APA contains no prohibitions on ex parte contacts between agency personnel and outside persons in notice-and-comment rulemaking”).

for rules to have the force of law, the Department of Homeland Security simply chose to issue a November 20, 2014, directive setting forth the provisions of DAPA (Deferred Action for Parents of Americans and Lawful Permanent Residents). There was no advance notice or comment – a violation found by the district court in the case.<sup>59</sup> When challenged over the circumvention of the notice and comment requirements, the Administration simply declared that the enormous program affecting the status of millions of undocumented person fell within an exception for “general statements of policy.” In other words, DAPA was merely treated as an exercise of discretionary policy where neither Congress nor the public would play a meaningful role. It is a striking example of how far we have strayed from the original model of our constitutional system. DAPA represents a type of government by memoranda where agencies simply issue new laws by executive fiat. The objection is not to the merits of the program, but the method chosen by the Administration (or any future administration). With the President in DAPA openly admitting that he is unilaterally ordering the very reforms that he was denied in Congress, the need for new procedural safeguards on agency action should be obvious. Regardless who may be the next president, federal legislative authority cannot be allowed to slip away into the mist of agency decision-making.

New APA procedures would help combat dangers of unilateral agency action as seen in *United States v. Texas*. However, that case showed how an agency can simply ignore relatively clear procedural requirements. A more robust and promising effort is found in reforms requiring legislative consent—an approach that I favor. Such an approach is found in the “Regulations from the Executive in Need of Scrutiny Act” or REINS.<sup>60</sup> REINS would require regulations to secure congressional approval in order to take effect. It would flip the dynamic of CRA from allowing congressional intervention to requiring congressional approval for major new rules. The law, however, has a default against new rule: if Congress does not act on a major rule within 70 days, it would be deemed “not approved” unless the president makes a determination that failure to enact the rule would harm the health, safety, or national security or cause conflicts with criminal law or treaty obligations. While there are good-faith objections to REINS as possibly curtailing executive authority and running afoul of cases like *Chadha*, I believe that the premise of the law is sound and compelling in asserting legislative authority over the law-making functions of agencies. I believe that a congressional approval law would be constitutional.<sup>61</sup> There are aspects of REINS that should be reexamined but the

<sup>59</sup> *Texas v. United States*, 86 F. Supp. 3d 591 (S.D. Tex. 2015); see also *Texas v. United States*, 787 F.3d 733 (5th Cir. 2015).

<sup>60</sup> See Regulations from the Executive in Need of Scrutiny (“REINS”) Act of 2011, H.R. 10, 112th Cong.; see also Regulatory Accountability Act of 2011, S. 1606, 112th Cong. (requiring regulators to adopt the “least costly” rule and imposing formal rulemaking procedures); Regulatory Accountability Act of 2011, H.R. 3010, 112th Cong. (same).

<sup>61</sup> *Immigration and Naturalization Service v. Chadha*, 462 U.S. 919 (1983), dealt with the one-house legislative veto. Obviously REINS avoids the bicameralism problem of a one-house veto and there is no reason why such a law cannot be crafted to avoid Presentment Clause problems. Notably, both Justice Stephen Breyer and Professor

categorical objection to such a law is fascinating. Indeed, the arguments from critics that the law would alter our constitutional structure only highlights how engrained the Administrative State has become in our assumptions about government. A REINS approach would be both constitutional and, if properly written, beneficial in reestablishing legislative authority.

Obviously, the easiest ways to prevent delegation rulings would be to expressly bar delegation or to impose clear limits. While distinguishing “strictly and exclusively legislative powers,” Chief Justice John Marshall, in *Wayman v. Southard*,<sup>62</sup> wrote for a unanimous Court in holding that Congress “may certainly delegate to others, powers which the legislature may rightfully execute itself.” The issue remained one of line drawing, for courts to isolate that point “which separates those important subjects, which must be entirely regulated by the legislature itself, from those of less interest, in which a general provision may be made, and power given to those who are to act under such general provisions, to fill up the details.”<sup>63</sup> This issue was in the forefront of the conflict between the Supreme Court and the White House during the 1930s, though admittedly the Court has routinely rejected nondelegation claims.<sup>64</sup> Yet, in 1928 in *J.W. Hampton, Jr. & Co. v. United States*, the Court upheld a statute that allowed the president to set tariffs because it contained an “intelligible principle” for implementing the statute.<sup>65</sup> Then, in 1935 in *A. L. A. Schechter Poultry Corp. v. United States*,<sup>66</sup> the Court struck down a provision of the National Industrial Recovery Act under the nondelegation doctrine for lacking such a principle. Likewise, *Panama Refining Co. v. Ryan*,<sup>67</sup> the Court held that no such principle was articulated when Congress gave the President authority to regulate the transportation of petroleum products.

In part, the association with the anti-New Deal cases contributed to the demise of the doctrine.<sup>68</sup> However, there was also a growing view that Congress could never practically address the myriad issues routinely addressed by agencies in the interpretation and enforcement of so many federal laws. The enactment in 1945 of the Administrative Procedure Act reflected this view by creating a quasi-legislative process for notice and comment on new federal rules. Past cases reaffirm that there is no inherent authority of agencies to carry out such actions and, as my colleague Dick Pierce noted, “an agency has the power to issue binding legislative rules only if and to the extent Congress has

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Lawrence Tribe have previously indicated that they also believed that such a law could be crafted to pass constitutional muster. See Stephen Breyer, *The Legislative Veto After Chadha*, 72 Geo. L.J. 785, 793-97 (1984); Laurence H. Tribe, *The Legislative Veto Decision: A Law by Any Other Name?*, 21 Harv. J. on Legis. 1, 19 (1984).

<sup>62</sup> 23 U.S. 1, 43 (1825).

<sup>63</sup> *Id.*

<sup>64</sup> Justice William Rehnquist invoked this doctrine in his opinion in *Industrial Union Department, AFL-CIO v. American Petroleum Institute (Benzene)*, 448 U.S. 607, 686 (1980) (Rehnquist, J., concurring). No other justice joined him in that position.

<sup>65</sup> *J.W. Hampton, Jr. & Co. v. United States*, 276 U.S. 394, 409 (1928).

<sup>66</sup> *A. L. A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

<sup>67</sup> *Panama Refining Co. v. Ryan*, 293 U.S. 388 (1935).

<sup>68</sup> JOHN HART ELY, *DEMOCRACY AND DISTRUST* 133 (1980).

authorized it to do so.”<sup>69</sup> Thus, even in carrying out the takeover of the steel mills during wartime, Justice Hugo Black demanded evidence of such congressional intent. Thus in *Youngstown Sheet & Tube Co. v. Sawyer*, he wrote:

The President’s power, if any, to issue the order must stem either from an act of Congress or from the Constitution itself. There is no statute that expressly authorizes the President to take possession of property as he did here. Nor is there any act of Congress to which our attention has been directed from which such a power can fairly be implied. Indeed, we do not understand the Government to rely on statutory authorization for this seizure.<sup>70</sup>

Professor Merrill has tried to thread this jurisprudential needle by moving beyond a nondelegation doctrine toward an “exclusive delegation doctrine” that states that “the President and executive branch agencies can subdelegate only if and to the extent Congress has authorized subdelegation. The exclusive delegation understanding tells us the Executive has no inherent authority to exercise legislative power.”

Whatever perspective is applied, the legislative functions of agencies are based either loosely or directly on a delegation theory. As a result, Congress could alter Section 706 of the APA<sup>71</sup> to expressly reject any presumption of delegation for such interpretations, particularly with regard to the jurisdiction of a federal office or agency. The section currently authorizes judicial review of agency actions to determine if the action is “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.” *Id.* The APA could be altered to expressly reject any claimed presumption of delegation and to reject the application of the *Chevron* standard absent an express standard of deference given to an agency. Section 701 already limits judicial review “(1) if a statute expressly precludes review or provides another form of review under the APA, that statute governs; or (2) the ‘agency action is committed to agency discretion by law.’” *Id.* § 701(a). Congress can change the APA to address the standard for review. Clearly if Congress can deny review, it can structure review under the belief that the lesser is contained in the greater in such use of congressional authority.

Putting aside the APA, Congress could also use a standard provision to add to statutes that expressly denies any delegation of authority to agencies to determine their jurisdiction. Such provisions could also deny any intended delegation over force of law interpretations while recognizing that provisions can be subject to a *Skidmore*-like standard of interpretation. Such standard clauses are already used for such legal issues as severability issues for judicial review. Courts could still evade such provisions but they will have to dispense with the pretense that the sweeping deference under *Chevron* is Congress’ doing or delegated intent. Such an affirmative denial of delegation should not be necessary. As the court in *United States v. Texas* noted, Congress “knows how to

<sup>69</sup> 1 KENNETH CULP DAVIS & RICHARD J. PIERCE, JR., ADMINISTRATIVE LAW TREATISE § 6.3, at 234 (3d ed. 1994)); *See also* Thomas W. Merrill, *Rethinking Article I, Section 1: From Nondelegation to Exclusive Delegation*, 104 COLUM. L. REV. 2097, 2109 (2004).

<sup>70</sup> *Youngstown Sheet & Tube Co. v. Sawyer*, 343 U.S. 579, 585 (1952).

<sup>71</sup> 5 U.S.C. § 706 (2012).

delegate discretionary authority” and courts should not presume such delegation.<sup>72</sup> However, an affirmative statement on nondelegation will reinforce such points in limiting the scope of agency action.

Finally, there is little question that Congress lacks the personnel and the time to directly monitor all of the decisions made in all of the federal agencies. As previously noted, congressional committees (and staff) should be significantly expanded to allow for greater monitoring of agency decisions. Our federal government is simply too large for Congress to act with regard to more than a relatively small fraction of agency actions. When Congress has faced areas with such limited ability to monitor or identify governmental abuse, it has used private attorneys general or citizen lawsuits. Congress should continue to ally itself with the public in monitoring agencies by creating such provisions to allow citizens to more easily pursue nondisclosures and noncompliance in court. It can further reinforce this system by examining new limitations placed on what constitutes a “prevailing party” for the purposes of recovery of fees and costs in such actions. It should also pursue amendments of laws that are information forcing, like the Freedom of Information Act, by addressing the long delays and expansive privileges imposed by agencies. In so doing, the public can help monitor and deter agency abuse.

#### IV. CONCLUSION

The notion of an Administrative State should be troubling to all members regardless of one’s party affiliation. The concern is not that we live in an “Age of Regulation,” which is and will remain an inevitable feature of modern government. Rather, it is the notion of a “state” unto itself that troubles some of us in watching the increasing independence and insularity of the agency system. As shown in the DAPA controversy, Congress has become merely one option for legislative changes in this new system. While the merits of a change like DAPA often obscures the constitutional implications of the method, the fact is the Congress is rapidly losing its relevance in such areas. While Madison hoped in *Federalist No. 51* that “ambition must . . . counteract ambition,” personal ambition can prevail over institutional interests in modern politics, as members become agents of their own obsolescence. I happen to agree with much of what these agencies are seeking to achieve and I will admit an academic identification with agency expertise. However, our system is premised on the notion that how we reach decisions is as important as what we decide. It is the process of resolution in the legislative process that brings stability to our system. It is often frustrating and, when the nation is divided, less gets done. However, the convenience of handing governing authority to federal agencies is no answer to our political divisions.

The separation of powers was intended first and foremost as a protection of individual liberty from the concentration of authority. It is easy to create a system that allows decisions to be made by an elite body. The Framers were all too aware of such a system in the form of a monarchy. They chose a system that was more difficult but more democratic in character. The accumulation of power in an agency rather than an individual is certainly different in character. It is more diffused and more difficult to discern. However, both forms of concentrated authority threaten the protections of

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<sup>72</sup> Texas v. United States, 86 F. Supp. at 658.

individual liberty. Indeed, the agency aggrandizement of power may be more dangerous in that it is more difficult to track and to challenge for individual citizens. Where the accumulation of power in an individual is called tyranny, the accumulation of power in agencies can become a type of technocracy where experts rule as benign lawgivers. This is not to suggest evil purpose or design. The motivations behind agency actions are generally positive. However, the Framers like Madison expressly rejected systems based on a presumption of good motivations. Indeed, some of the worst actions taken in our country have been justified by the best of motivations. As the great Louis Brandeis warned in his dissent in *Olmstead v. United States*,<sup>73</sup> where he warned that the “greatest dangers to liberty lurk in insidious encroachment by men of zeal, well meaning but without understanding.”

Thank you again for the honor of addressing the Committee today. I am happy to answer any questions that you may have.

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<sup>73</sup> 277 U.S. 438 (1928).



**Testimony of Randolph J. May**

**President, The Free State Foundation**

**Hearing on “The Administrative State: An Examination of  
Federal Rulemaking”**

**before the**

**Committee on Homeland Security and Governmental Affairs**

**United States Senate**

**April 20, 2016**

**Summary of the Testimony of Randolph J. May  
President, The Free State Foundation**

The Committee's identification of the Federal Communications Commission's net neutrality rule as deserving of examination is wise. The Commission's rulemaking is instructive regarding the ways in which a faulty rulemaking process enables the growth of the burgeoning administrative state and adversely impacts the economy – while, at the same time, compromising rule of law norms. I want to highlight four areas in which the FCC's net neutrality rulemaking is problematic.

First, the net neutrality rulemaking truly is a case of the proverbial “solution in search of a problem.” Or as FCC Commissioner Ajit Pai put it recently, the rule “was a 313-page solution that wouldn't work to a problem that didn't exist.” To put it bluntly, in this case there was no meaningful evidence of an existing market failure or consumer harm that required the Commission to adopt rules applying Ma Bell-era Title II public utility-like regulation to today's Internet service providers. The dynamic, competitive marketplace in which Internet service providers operate today is far removed from the staid monopolistic markets for which public utility-type regulation was devised.

Second, as a result of the direct and indirect costs and burdens imposed on Internet service providers, the rule's adoption most likely will have a deleterious economic impact by chilling investment and innovation. Indeed, there is some persuasive evidence that it is already doing so. Of course, diminished investment and innovation mean diminished jobs and consumer welfare.

Third, at a minimum, the manner of President Obama's direct involvement in the FCC's net neutrality rulemaking, and the aftermath of his involvement that resulted initially in confusion at the Commission and then, shortly afterward, in an abrupt change in course, raise questions about the FCC's supposed independence. The manner in which the rulemaking was conducted serves to undermine the notion that the FCC's decisions are primarily based on its specialized communications law and policy expertise rather than political considerations. And this, in turn, jeopardizes the public's confidence in the soundness of the Commission's decisions and the agency's institutional integrity. Just last week, the White House released a high-profile statement urging the FCC to adopt a specific course of action in the agency's controversial video navigation device rulemaking. Repeated high-profile presidential interventions like this further undermine the notion that the FCC acts independently and free from executive branch control.

Finally, aside from issues relating to President Obama's involvement, there are aspects of the net neutrality rule, specifically including the vague general conduct standard and the enforcement regime the rule creates, that call into question compliance with accepted rule of law and due process norms. These norms require that law be predictable and knowable in advance of the imposition of sanctions, which in the case of the net neutrality rule is not the case. Failing to adhere to these norms also threatens to undermine the public's confidence in the agency's institutional integrity.



**Testimony of Randolph J. May****President, The Free State Foundation**

Mr. Chairman, Ranking Member Carper, and Members of the Committee, thank you for inviting me to testify. I am President of The Free State Foundation, a non-profit, nonpartisan research and educational foundation located in Rockville, Maryland. The Free State Foundation is a think tank that, among other things, focuses its research in the communications law and policy and administrative law and regulatory practice areas. I have been involved for almost forty years in communications law and policy in various capacities, including having served as Associate General Counsel at the Federal Communications Commission. While I am not speaking on behalf of these organizations, by way of background I note that I am a past Chair of the American Bar Association's Section of Administrative Law and Regulatory Practice and its representative in the ABA House of Delegates. I am currently a Public Member of the Administrative Conference of the United States and a Fellow at the National Academy of Public Administration. So, today's hearing on the Administrative State and rulemaking, which includes a specific focus on the FCC, is at the core of my longstanding experience and expertise in communications law and policy and administrative law.

**I. The Administrative State Today: A Brief Overview**

Given the increase in regulatory activity during the years of the Obama Administration, it is certainly fitting to examine the ongoing expansion of the administrative state, and the role that rulemaking and related regulatory activities play in

impacting our personal lives, our families, and, importantly, our nation's economy. As Chief Justice John Roberts declared in 2013 in his opinion in *City of Arlington v. Federal Communications Commission*, "[t]he administrative state 'wields vast power and touches almost every aspect of daily life.'"<sup>1</sup> He observed that the agencies which comprise today's administrative state typically combine legislative, executive, and judicial powers in one body, despite James Madison's warning in Federalist No. 47 that lodging these powers "in the same hands . . . may justly be pronounced the very definition of tyranny." Not all of the 440 agencies listed in the Federal Register possess the authority to promulgate rules that have the force of law – so-called legislative rules – but many do.<sup>2</sup> In any event, as Chief Justice Roberts recognized, the accumulation of powers in the nation's federal agencies is no longer an exception to the original constitutional plan, "it is a central feature of modern American government."<sup>3</sup>

There is a rich literature on the vast domain of today's administrative state and its expansion in recent years, and there is no need here to belabor the data.<sup>4</sup> But a few facts and figures are useful to provide context for today's hearing. In 2014, federal regulation and intervention cost American consumers and businesses an estimated \$1.88 trillion in lost economic productivity and higher prices. This amounts to an average of \$14,976 for each American household's share of the economy-wide regulatory costs assuming these costs are passed along to consumers.

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<sup>1</sup> *City of Arlington v. FCC*, 133 S. Ct. 1863, 1878 (2013), quoting *Free Enterprise Fund v. Public Company Accounting Oversight Bd.*, 561 U.S. 477 (2010).

<sup>2</sup> For a list of the 440 agencies, see the Federal Register, available at: <https://www.federalregister.gov/agencies> (accessed on April 9, 2016).

<sup>3</sup> *City of Arlington*, at 1878.

<sup>4</sup> The figures in this paragraph and the next are taken from Clyde Wayne Crews, *Ten Thousand Commandments 2015*, Competitive Enterprise Institute (2015). I gratefully acknowledge the contribution of his annual *Ten Thousand Commandments* series.

In 2014 alone, 3554 rules were issued by federal agencies. Of the 3415 regulations then in the pipeline, 200 were deemed “economically significant,” meaning each of the 200 was estimated to have at least a \$100 million impact on the economy; 674 were identified as affecting small businesses. As but one indication of the increase in regulatory activity during the Obama Administration years, of the six all-time highest Federal Register page counts, five have occurred, thus far, under President Obama.

## **II. The Federal Communications Commission: An Agency Bent on Maintaining and Expanding Its Regulatory Power**

While there are other rich targets worthy of consideration in connection with an examination of the exercise of an agency’s rulemaking authority, the Federal Communications Commission certainly deserves attention, and the remainder of my testimony will be focused on the FCC. Aside from the impact its actions may have, say, on non-economic matters such as First Amendment free speech rights and individual liberty, the communications and Internet sectors, which in one way or the other, are within the FCC’s (asserted) regulatory ambit, comprise approximately one-sixth of the nation’s annual economic output. This alone makes the FCC’s actions worthy of review.

In hearings before the House Subcommittee on Communications and Technology in 2011 and 2013, concerning reform of the FCC’s processes,<sup>5</sup> I set the stage for my testimony by quoting from a strategic plan entitled, “A New FCC for the 21<sup>st</sup> Century,” released by then-FCC Chairman William Kennard in August 1999. The plan’s first three sentences read:

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<sup>5</sup> Reforming FCC Process: Hearing Before the Subcomm. on Commc’ns & Tech. of the H. Comm. on Energy & Commerce (2011)(statement of Randolph J. May); Improving FCC Process: Hearing Before the Subcomm. on Commc’ns & Tech. of the H. Comm. on Energy & Commerce (2013) (statement of Randolph J. May).

In five years, we expect U.S. communications markets to be characterized predominately by vigorous competition that will greatly reduce the need for direct regulation. The advent of Internet-based and other new technology-driven communications services will continue to erode the traditional regulatory distinctions between different sectors of the communications industry. As a result, over the next five years, the FCC must wisely manage the transition from an industry regulator to a market facilitator.<sup>6</sup>

Chairman Kennard was proved right. The communications marketplace incontrovertibly is characterized by much more marketplace competition and technological dynamism now than in 1999. Economists and regulatory experts universally agree that increased marketplace competition should, at least to some meaningful extent, supplant the need for regulation. This is because the marketplace competition serves to protect consumers and does so more efficiently and effectively – that is, by imposing less costs on the nation’s economy – than regulation. But rather than transitioning to an agency fit for the 21<sup>st</sup> Century’s competitive communications and Internet marketplace, as the 1999 strategic plan envisioned, the FCC, especially during the Obama Administration’s years, has exercised its rulemaking authority in ways that make it every bit as much of an “industry regulator” now as it was in 1999.

Not coincidentally, the number of final rules issued by the FCC increased from 109 in 2012 to 144 in 2014 – and there has been no slowdown in rulemaking activity involving major matters in 2015 and this year. The FCC will spend an estimated \$545 million on regulatory development and enforcement during FY 2016,<sup>7</sup> and the agency routinely accounts for several rules in the pipeline with an estimated \$100 million in annual economic impact.

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<sup>6</sup> FCC, “Strategic Plan, A New FCC for the 21<sup>st</sup> Century,” August 1999, available at: [https://transition.fcc.gov/21st\\_century/draft\\_strategic\\_plan.pdf](https://transition.fcc.gov/21st_century/draft_strategic_plan.pdf) (accessed April 9, 2016).

<sup>7</sup> Susan Dudley and Melinda Warren, Regulators’ Budget No. 37, May 19, 2015, Table A-1, p. 17, available at: [https://wc.wustl.edu/files/wc/imce/2016\\_regulators\\_budget\\_final.pdf](https://wc.wustl.edu/files/wc/imce/2016_regulators_budget_final.pdf) (accessed April 9, 2016.)

### **III. The FCC's Net Neutrality Rule: A Case Study in a Faulty Rulemaking Process and the Consequences**

Although there are many other FCC rulemakings worthy of study (for example, at present, the agency's set-top box video navigation device and privacy rulemakings deserve close scrutiny), as requested by the Committee, I will focus the remainder of my testimony on the Commission's net neutrality rule.<sup>8</sup> (The Commission refers to it as the "Open Internet" rule, but I prefer to call it, more properly I think, the "Internet Regulation" rule.) The Committee's identification of the net neutrality rule as deserving of examination is wise because the rulemaking is instructive regarding the ways in which a faulty rulemaking process enables the growth of burgeoning administrative state and adversely impacts the economy – while, at the same time, compromising rule of law norms.

First, the net neutrality rulemaking truly is a case of the proverbial "solution in search of a problem." Or as FCC Commissioner Ajit Pai put it recently, the rule "was a 313-page solution that wouldn't work to a problem that didn't exist."<sup>9</sup> To put it bluntly, in this case there was no meaningful evidence of an existing market failure or consumer harm that required the Commission to adopt rules applying Ma Bell-era public utility-like regulation to today's Internet service providers. The dynamic, competitive marketplace in which Internet service providers operate today is far removed from the staid monopolistic markets for which public utility-type regulation was devised.

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<sup>8</sup> "Protecting and Promoting the Open Internet," Report and Order on Remand, Declaratory Ruling, and Order, GN Docket No. 14-28, released March 12, 2015.

<sup>9</sup> "The FCC and Internet Regulation: A First-Year Report Card," Remarks of FCC Commissioner Ajit Pai before the Heritage Foundation, February 26, 2016.

Second, as a result of the direct and indirect costs and burdens imposed on Internet service providers, the rule's adoption most likely will have a deleterious economic impact by chilling investment and innovation. Indeed, there is some persuasive evidence that it is already doing so. Of course, diminished investment and innovation mean diminished jobs and consumer welfare.

Third, at a minimum, the manner of President Obama's direct involvement in the FCC's net neutrality rulemaking, and the aftermath of his involvement that resulted initially in confusion at the Commission and, shortly afterward, in an abrupt change in course, raise questions about the FCC's supposed independence. The manner in which the rulemaking was conducted serves to undermine the notion that the FCC's decisions are largely based on its specialized communications law and policy expertise rather than political considerations.<sup>10</sup> And this, in turn, jeopardizes the public's confidence in the soundness of the Commission's decisions and the agency's institutional integrity. Just last week, the White House released a high-profile statement urging the FCC to adopt a specific course of action in the Commission's controversial video device navigation rulemaking. Repeated high-profile presidential interventions like this further undermine the notion that the FCC acts independently and free from executive branch control.

Finally, entirely aside from issues relating to President Obama's involvement, there are aspects of the net neutrality rule, specifically including the vague general conduct standard and the enforcement regime the rule creates, that call into question compliance with accepted rule of law and due process norms that require that law be predictable and knowable in advance of the imposition of sanctions, which in the case of

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<sup>10</sup> See "Regulating the Internet: How the White House Bowled Over FCC Independence," A Majority Staff Report of the Committee of Homeland Security and Governmental Affairs, United States Senate, February 29, 2016.

the net neutrality rule is not the case. This too threatens to undermine the public's confidence in the agency's institutional integrity.

I will now say more about each of these problematic areas in turn.

#### A. "A Solution in Search of a Problem"

In the net neutrality rulemaking, after President Obama's unusual involvement in the proceeding,<sup>11</sup> the FCC abandoned the primary approach it had outlined in its *Notice of Proposed Rulemaking*<sup>12</sup> and instead adopted rules that imposed a public utility-like regime on today's broadband Internet service providers ("ISPs"). In opting to classify broadband Internet service providers as "telecommunications carriers" rather than "information service" providers, the Commission subjected them to the same Title II<sup>13</sup> common carrier regulatory regime initially applied to railroads in 1887 by the Interstate Commerce Act and to monopolistic Ma Bell in 1934 by the Communications Act of 1934. At bottom, the most troublesome aspect of the FCC's net neutrality rulemaking is the fact that the Commission acted without any meaningful evidence of existing market failure in the Internet services marketplace or evidence of consumer harm. The Commission cited only three or four anecdotal instances throughout the 313-page order of ISP practices that might possibly have caused consumer harm. There certainly was no effort to conduct a meaningful cost-benefit analysis before adopting the rules.

Instead, the whole rulemaking exercise was premised on the existence of hypothetical harms that the Commission imagined "might" or "could" occur. Even a

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<sup>11</sup> I will address President Obama's involvement in more detail below.

<sup>12</sup> "Protecting and Promoting the Open Internet," Notice of Proposed Rulemaking, GN Docket No. 14-28, released May 15, 2014.

<sup>13</sup> Title II ("Common Carriers") is the title of the Communications Act of 1934 that applies the traditional common carrier regulatory scheme to service providers classified as telecommunications carriers.

casual perusal of the order reveals hundreds of pure FCC conjectures about what *could* or *might* occur absent adoption of new regulations, not credible evidence of actions that actually had occurred.<sup>14</sup> The Commission failed to engage in any real market power analysis. Instead, it was content to rely on bandying about a “gatekeeper” label to the Internet providers based merely on the assertion that ISP customers might (but not necessarily would) experience some difficulties or incur some costs in switching from one ISP to another. Of course, this is true in many other functioning markets as well.

I don’t want to address all of the arguments here concerning the Commission’s asserted lack of legal authority to act as it did. The challenge to the FCC’s action is pending before the D.C. Circuit Court of Appeals, and a decision may be issued at any time. I will just say here that, given the absence of meaningful evidence of any present market failure or consumer harm, the Commission’s decision to reverse its previous policy of not applying Title II public utility regulation to ISPs – which it defended, successfully, all the way to the Supreme Court in 2005<sup>15</sup> – flouts Congress’s declaration that it is the policy of the United States “to preserve the vibrant and competitive free market that presently exists for the Internet and other interactive computer services, unfettered by Federal or State regulation.”<sup>16</sup>

#### **B. The Net Neutrality Rule’s Deleterious Economic Impact**

Of course, there are many rules, especially health and safety regulations, that admittedly impose costs on the economy but that nevertheless are justified by their asserted benefits. I do not want to be understood as arguing against all federal regulation,

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<sup>14</sup> Indeed, as an indication of the conjectural nature of the Commission’s reasoning regarding evidence of harm resulting from ISP practices, the majority’s order employed the speculative “might” and “could” over 250 times in the order.

<sup>15</sup> Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs. 545 U.S. 967 (2005).

<sup>16</sup> Communications Act of 1934, as amended, Section 230(b)(2), 47 U.S.C. §230(b)(2).



or all FCC regulation. But in the case of the net neutrality rule, not only was there no evidence concerning the existence of an existing market failure, there was affirmative evidence that the costs imposed by the new regulations likely would impair investment and innovation. There are direct costs imposed by the net neutrality rule, such as increased operating expenses relating to compliance with additional regulatory obligations. And there are indirect costs related to less easily measurable, but nonetheless real, items such as foregone business opportunities attributable to the regulatory uncertainty created by many aspects of the new rule and the employment and consumer welfare losses stemming from the reductions in investment and innovation.<sup>17</sup>

Many commenters, including the Free State Foundation, asserted in the Commission's rulemaking proceeding, that the direct and indirect costs imposed by the burdensome new regulations likely would chill future facilities investment by broadband ISPs<sup>18</sup> – a contention consistent with the prevailing economic literature. While it may be some time before more definitive data become available, early indications are that the FCC's rule already is having a chilling impact on ISP capital investment. Hal Singer, a respected economist affiliated with the Progressive Policy Institute, has estimated that the capital expenditures of the twelve largest ISPs declined by \$240 million in 2015 from the 2014 level, a 0.4% year-over-year reduction. Only twice before have the capex investments of broadband providers declined, once after the dot-com bust in 2000 and in 2008 at the beginning of the financial crisis. In his report on the 2015 investment results, Mr. Singer states:

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<sup>17</sup> I will discuss below the problematic nature of one particular aspect of the uncertainty created by the net neutrality rule in relation to compromising rule of law norms.

<sup>18</sup> There is little or no dispute that in the fifteen years prior to the adoption of the FCC's net neutrality order the private sector invested approximately \$1.3 trillion in building out broadband networks.

This is not to conclude that Title II solely caused capital expenditures to stagnate. Several factors could be at play. But when investment theory is corroborated by evidence, as it is here, it is reasonable to infer that reclassification of ISPs as Title II common carriers was not a good thing for investments. The theory provides a crisp prediction: Reclassification is a prerequisite for price regulation and mandatory unbundling, both of which are recognized in the economics literature...to cause capital flight.<sup>19</sup>

Of course, the disincentive to investment extends far beyond the twelve largest ISPs, although they admittedly account for a large portion of total ISP capital expenditures. FCC Commissioner Ajit Pai has detailed the adverse impact on some smaller ISPs around the country. There are documented instances of these smaller ISPs scaling back facilities investment and discontinuing plans to extend broadband service to unserved communities.<sup>20</sup> At the Free State Foundation's Eighth Annual Telecom Policy Conference held on March 23, 2016, Glenn Lurie, President & CEO, AT&T Mobility and Consumer Operations, stated that the FCC's net neutrality rule negatively impacted AT&T's investment plans for its broadband network in the United States. In answering a question, Mr. Lurie explained that, in light of the FCC's net neutrality order, AT&T has "invested in a whole bunch of other things," such as DIRECTV and overseas businesses, such as in Mexico.<sup>21</sup>

It bears emphasis that it is difficult to measure with any precision the adverse economic impact of foregone business opportunities by the ISPs and foregone productivity increases that are lost as a result diminished investment and innovation. But

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<sup>19</sup> Hal Singer, "ISP Capital Expenditures in the Title II Era," available at: [-the-title-ii-era-4q-edition/" https://haljsinger.wordpress.com/2016/02/24/isp-capital-expenditures-in-the-title-ii-era-4q-edition/](https://haljsinger.wordpress.com/2016/02/24/isp-capital-expenditures-in-the-title-ii-era-4q-edition/) (accessed April 11, 2016.)

<sup>20</sup> See "The FCC and Internet Regulation: A First-Year Report Card," Remarks of FCC Commissioner Ajit Pai before the Heritage Foundation, February 26, 2016, at page 2.

<sup>21</sup> "Something Isn't Right – Wheeler Wrong on AT&T Investment Post-Net Neutrality Order," Communications Daily, March 24, 2016.

it already looks like the decline in ISP investment is measurable. And even if it turns out to be only a decline in the rate of investment that otherwise would occur, the loss to the nation's economy will amount to tens of billions of dollars over the next few years. Of course, this loss to the economy translates into a real loss in jobs.

**C. The FCC's Supposed Independence Was Compromised by President Obama's Involvement and the Agency's Abrupt Change of Course**

At a minimum, the manner of President Obama's involvement in the FCC's net neutrality rulemaking and the aftermath at the agency of his involvement raise questions about the FCC's supposed independence and serve to undermine the notion that its decisions are largely based on its specialized expertise regarding communications law and policy. I want to state at the outset of this discussion that it is not my position that it is improper or inappropriate for executive branch officials, including the President, to present their views to the FCC in a rulemaking proceeding. The problem in this case arises from the timing and overall context of the manner in which the President's involvement occurred.

The FCC, like the Securities Exchange Commission and the Federal Trade Commission and other similar multimember agencies, are commonly considered independent agencies. They are comprised of commissioners who serve fixed, staggered terms. Significantly, there may be no more than a bare majority of commissioners from the same political party, which, for the FCC, means that no more than three of the five commissioners may be from the same party. These are the primary indicia intended to

give the FCC and similarly structured agencies a measure of independence and insulation from political control that differs from that accorded to executive branch agencies.<sup>22</sup>

Ever since the Supreme Court in 1935 held in *Humphrey's Executor v. United States* that at least certain “good cause” limitations on the President’s power to remove a member of the Federal Trade Commission (“FTC”) were constitutional, agencies such as the FTC and the FCC have been considered, in at least some good measure, as a matter of law and established practice, “free from executive control.”<sup>23</sup> According *Humphrey's Executor*, as a predominantly quasi-legislative and quasi-judicial body, the FTC “is charged with the enforcement of no policy except the policy of the law”<sup>24</sup> and “[i]ts duties are neither political nor executive.”<sup>25</sup> As such, the agency “cannot in any proper sense be characterized as an arm or an eye of the executive.”<sup>26</sup> Rather, Congress intended “to create a body of experts who shall gain experience by length of service - a body which shall be independent of executive authority, *except in its selection*, and free to exercise its judgment without the leave or hindrance of any other official or any department of the government.”<sup>27</sup>

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<sup>22</sup> The independents are sometimes characterized as the “headless fourth branch” of government. The original reference to the “headless fourth branch” usage is from THE PRESIDENT’S COMMITTEE ON ADMINISTRATIVE MANAGEMENT, REPORT OF THE COMMITTEE WITH STUDIES OF ADMINISTRATIVE MANAGEMENT IN THE FEDERAL GOVERNMENT (1937), reprinted in SUBCOMMITTEE ON SEPARATION OF POWERS, COMMITTEE ON THE JUDICIARY, U.S. SENATE, SEPARATION OF POWERS AND THE INDEPENDENT AGENCIES: CASES AND SELECTED READINGS, 91st Cong., 1st Sess. 345 (1969). For a useful scholarly study containing information on almost all independent agencies, see Marshall J. Breger & Gary J. Edles, *Established by Practice: The Theory and Operation of Independent Federal Agencies*, 52 ADMIN. L. REV. 1111 (2000).

<sup>23</sup> *Humphrey's Ex'r v. United States*, 295 U.S. 602, 628 (1935).

<sup>24</sup> *Id.*, at 624.

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*, at 628.

<sup>27</sup> *Id.*, at 625-26 (emphasis in original.) For further reading, I discussed *Humphrey's Executor* and the independent agencies at much greater length in Randolph J. May, *Defining Deference Down: Independent Agencies and Chevron Deference*, 58 ADMIN. L. REV. 429 (2006), and Randolph J. May, *Defining Deference Down, Again: Independent Agencies, Chevron Deference, and Fox*, 62

The Court’s analysis, based primarily on the characteristics of the multimember agencies set forth above – fixed, staggered terms and bipartisan membership – should apply to the FCC as well. Indeed, when the Federal Radio Commission was created in 1927, the direct predecessor agency of the FCC that was created with the same structure, the Senate Committee on Interstate Commerce’s report declared that the agency’s regulatory authority should be placed in the hands of “one independent body”<sup>28</sup> that would become “an expert authority.”<sup>29</sup>

In the net neutrality rulemaking, as the *Wall Street Journal* reported in a lengthy investigative story, the President’s open involvement in the proceeding came “after an unusual, secretive effort inside the White House, led by two aides who built a case for the principle known as ‘net neutrality’ through dozens of meetings” with online activists and others favoring the Title II public utility approach. The *Journal* reported that the White House acted “like a parallel version of the FCC itself.”<sup>30</sup> After the secretive White House process, on November 10, 2014, President Obama issued a public announcement and accompany video urging the FCC to adopt the Title II regulatory approach.<sup>31</sup> He ended his statement by “ask[ing] them [the Commissioners] to adopt the policies I have outlined here.”<sup>32</sup> At the Commission meeting in February 2016, the three Democrat commissioners did exactly what the President asked them to do in his statement, while the two Republicans dissented.

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ADMIN. L. REV. 433 (2010).

<sup>28</sup> S. REP. NO. 69-772, at 2 (1926)

<sup>29</sup> S. REP. NO. 69-772, at 2-3 (1926).

<sup>30</sup> Gautham Nagesh & Brody Mullins, How White House Thwarted FCC Chief on Internet Rules, WALL ST. J., Feb. 4, 2015.

<sup>31</sup> WHITE HOUSE, November 2014 The President’s message on net neutrality, <https://www.whitehouse.gov/net-neutrality>.

<sup>32</sup> *Id.*

On February 29, 2016, the majority staff of this Committee released a report detailing the secret White House meetings; the briefing FCC Chairman Wheeler received from Jeffrey Zients, President Obama's economic advisor, shortly before President Obama's public announcement; President Obama's announcement; and the ensuing FCC staff confusion followed soon thereafter by an abrupt change of direction in the draft proposal to conform it to President Obama's "ask."<sup>33</sup> Relying on the discovery of Commission emails and other documents, the majority staff report sets forth what transpired, and I see no need to burden my testimony by repeating here the information contained in the report. Rather, I want to offer some brief observations, based on my decades of experience observing the FCC, in conjunction with my administrative law expertise, regarding the troublesome nature of the process as it unfolded.

As was common knowledge based on press reports at the time, and as this Committee's majority staff report confirms based on an examination of Commission emails, the FCC staff, at Chairman Wheeler's direction, already had produced a draft order, which was about to be circulated to the other commissioners, that opted for the less stringent, more flexible "commercially reasonable" approach under Section 706 of the Communications Act rather than the Title II common carrier approach ultimately adopted. While not absolutely foreclosing consideration of Title II regulation, the Commission had tentatively concluded in the May 2014 *Notice of Proposed Rulemaking* that it would rely on the less rigid Section 706. The *Notice* gave short shift to the Title II option.

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<sup>33</sup> See "Regulating the Internet: How the White House Bowled Over FCC Independence," A Majority Staff Report of the Committee of Homeland Security and Governmental Affairs, United States Senate, February 29, 2016.

In my view, as a matter of sound process and in order to maintain its credibility as an independent agency, the Commission should have issued a *Further Notice* calling for another round of public comments after President Obama's announcement before abruptly abandoning the approach already embodied in the nearly completed draft order. Chairman Wheeler rejected allowing another comment round, although interested parties continued to offer views through *ex parte* meetings. Unfortunately for the Commission and the public, the manner in which the rulemaking was conducted created the widespread impression of an agency ultimately relying on political considerations rather than on its own presumed expertise. This impression diminishes public confidence in the integrity of the Commission's process and the soundness of its decisions.

In a *Perspectives from FSF Scholars*, Enrique Armijo, a law school professor and member of the Free State Foundation's Board of Academic Advisors, summed up what had occurred this way:

[Y]ou should find this level of politicization of an independent agency rulemaking deeply troubling. The rulemaking process is expressly intended to insulate federal agencies from the political winds, and designed to give agency deliberations and interested parties' positions an open airing. And secretly held, off-the-record meetings in another part of the Executive Branch concerning pending agency action, the results of which are adopted by the agency itself as its final rule, are in headlong conflict with that approach.<sup>34</sup>

Professor Armijo concluded that if evidence developed in the rulemaking process regarding investment incentives, technological feasibility, or the like "can be trumped

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<sup>34</sup> Enrique Armijo, Net Neutrality, "Administrative Procedure, and Presidential Overreach," *Perspectives from FSF Scholars*, Vol. 10, No. 39, November 19, 2015, at 2, available at: [http://freestatefoundation.org/images/Net\\_Neutrality,\\_Administrative\\_Procedure,\\_and\\_Presidential\\_Overreach\\_111915.pdf](http://freestatefoundation.org/images/Net_Neutrality,_Administrative_Procedure,_and_Presidential_Overreach_111915.pdf) (accessed April 10, 2016). It's worth noting that Professor Armijo stated that he "personally would likely conclude some form of net neutrality rules are a net benefit for Internet users." Nevertheless, as he explains, he finds the process employed in adopting the net neutrality rule highly problematic.

or cancelled out by a presidential statement delivered at the 11<sup>th</sup> hour of a years-long rulemaking proceeding, any decent administrative law attorney would have to consider advising the client to save its money – or to spend it on lobbying the White House instead.”<sup>35</sup> This is a sad commentary on the FCC’s net neutrality rulemaking process with which I concur.<sup>36</sup>

#### **D. The Net Neutrality Rule Compromises Basic Rule of Law Principles**

There are many substantive reasons why the Commission’s net neutrality order is problematic as a matter of policy and law, too many to rehearse them all here.<sup>37</sup> Rather, in this final section, I intend to highlight one key aspect of the agency’s order that is particularly troublesome from a rule of law perspective. Contrary to Chairman Wheeler’s assertion, the FCC’s order does not provide certainty. Indeed, by its very nature, it necessarily generates uncertainty. And this built-in uncertainty – apart from the economic harms it creates by chilling investment and innovation – creates a rule of law problem with regard to the order’s enforcement.

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<sup>35</sup> Id., at 3.

<sup>36</sup> It is worth noting that the form of the President’s intervention, with the publicized video, was in and of itself unusual. In the past, the executive branch typically made its views known to the FCC through formal comments and letters submitted by the Department of Commerce’s National Telecommunications and Information Administration during the course of the public comment process. Confirming to this traditional, less sensational manner of making the President’s views known is likely to be more conducive to maintaining a rulemaking environment in which the agency’s independence does not appear to be compromised or the role of its presumed expertise diminished.

<sup>37</sup> As a matter of policy, but for one example, see Randolph J. May, “Thinking the Unthinkable: Imposing the ‘Utility Model’ on Internet Providers,” Perspectives from FSF Scholars, September 29, 2014, available at: [http://freestatefoundation.org/images/Thinking\\_the\\_Unthinkable\\_092914.pdf](http://freestatefoundation.org/images/Thinking_the_Unthinkable_092914.pdf) (accessed April 14, 2016). And, as a matter of law, but for one example, see Randolph J. May, “Why Chevron Deference May Not Save the FCC’s Open Internet Order – Part I” Perspectives from FSF Scholars, April 23, 2015, available at: [http://freestatefoundation.org/images/Why\\_Chevron\\_Deference\\_May\\_Not\\_Save\\_the\\_FCC\\_s\\_Open\\_Internet\\_Order\\_-\\_Part\\_I\\_042315.pdf](http://freestatefoundation.org/images/Why_Chevron_Deference_May_Not_Save_the_FCC_s_Open_Internet_Order_-_Part_I_042315.pdf) (accessed April 14, 2016).



The net neutrality rule establishes what the Commission calls three “bright-line” rules prohibiting broadband Internet service providers from “blocking” or “throttling” Internet traffic or engaging in “paid prioritization.”<sup>38</sup> I very seriously doubt that even these supposed bright-line prohibitions will be free, over time, from ambiguities as to their meaning. In any event, this definitely is not the case for another prohibition, a “general conduct standard” that the Commission itself calls a “catch all.”<sup>39</sup> This conceded “catch all” standard provides that an ISP “shall not unreasonably interfere with or unreasonably disadvantage” end users or “edge” content or application providers.<sup>40</sup>

The elastic nature of the inherently vague “no unreasonable interference/disadvantage” catch-all gives agency officials nearly unbounded discretion to determine that an Internet provider should be punished for violating the rule. The problem, of course, is that the catch-all provision – grounded as it is only in “reasonableness” – does not provide, in advance, a knowable, predictable rule consistent with due process and rule of law norms.<sup>41</sup> And the fact that the entire Internet ecosystem is so dynamic, with both technology and business models changing at a fast-paced rate in response to quickly evolving consumer demands, compounds the difficulty confronting Internet service providers. As they contemplate new services and features to distinguish

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<sup>38</sup> Open Internet Order, at paras. 14-19.

<sup>39</sup> *Id.*, at para. 21.

<sup>40</sup> *Id.*

<sup>41</sup> The Commission provided what it called a “non-exhaustive” list of seven factors that it said it would use to assess the reasonableness of Internet provider practices. But highlighting the elasticity and vagueness of the catch-all provision, the Commission emphasized that, in addition to the non-exhaustive list, “there may be other considerations relevant to determining whether a particular practice violates the no-unreasonable interference/disadvantage standard.” *Id.*, at para. 138.

their offerings from their competitors,<sup>42</sup> Internet providers are put in the position of guessing whether the Commission's view of reasonableness will comport with their own. This surely is not a recipe for the "permissionless innovation" regime that FCC Chairman Wheeler likes to tout.<sup>43</sup> Rather, to put it in standard administrative law terms, it is an invitation for arbitrary and capricious rulings by government officials who may be disposed to exercise their "catch all" discretion to favor some regulated parties over others. This is the opposite of "permissionless innovation."

To compound matters even further, the Commission delegated authority to enforce the "catch all" general conduct standard in the first instance to the agency's Enforcement Bureau staff.<sup>44</sup> As if to concede the inherent vagueness built into the new general conduct standard, the Commission delegated authority to the Enforcement Bureau staff to establish a cumbersome, complex process by which private parties can seek "advisory opinions" that may not even be binding in any event.<sup>45</sup> The establishment of the elaborate new regime for seeking advisory opinions regarding the lawfulness of

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<sup>42</sup> The Commission is investigating various new zero-rating and sponsored data plans offered by wireless carriers under the general conduct standard, even though these new offerings, such as T-Mobile's Binge On plan, appear to be very popular with consumers. The zero-rating and sponsored data plans, in one way or another, allow consumers to access various content and applications without such usage counting towards data limits or incurrance of otherwise applicable data charges.

<sup>43</sup> Statement of Chairman Tom Wheeler, Protecting and Promoting the Open Internet, Gen Docket No. 14-28, available at: [c/attachmatch/FCC-15-24A2.pdf](https://apps.fcc.gov/edocs_public/attachmatch/FCC-15-24A2.pdf), [https://apps.fcc.gov/edocs\\_public/attachmatch/FCC-15-24A2.pdf](https://apps.fcc.gov/edocs_public/attachmatch/FCC-15-24A2.pdf) ("These enforceable, bright-line rules assure the rights of Internet users to go where they want, when they want, and the rights of innovators to introduce new products without asking anyone's permission."); John Eggerton, "FCC's Wheeler and the 'Common Good' Standard," *Broadcasting & Cable*, November 4, 2015. ("Wheeler said the new rules were all about stimulating 'permissionless innovation.'").

<sup>44</sup> Of late, the staff has proven to be especially aggressive in imposing large fines on regulated parties for actions that (as shown below) arguably were not known in advance to be unlawful. Margaret Harding McGill, "GOP Criticism Unlikely to Deter Aggressive FCC Enforcement," *Law 360*, November 25, 2015.

<sup>45</sup> Open Internet Order, at paras. 228-239.

proposals for new services is a good indication that “permissionless innovation” won’t prevail.

In short, the amorphous “general conduct standard,” which is at the heart of the net neutrality rule, implicates fundamental rule of law norms and leads to arbitrary and capricious decisions. Friedrich Hayek, in his famous work, *The Road to Serfdom*, declared the rule of law “means the government in all its actions is bound by rules fixed and announced beforehand – rules which make it possible to see with fair certainty how the authority will use its coercive powers in given circumstances and to plan one’s individual affairs on the basis of this knowledge.”<sup>46</sup> *Federalist No. 62* (probably authored by James Madison) addresses the “calamitous” effects of mutable policy resulting from incoherent laws. The author declares: “Law is defined to be a rule of action; but how can that be a rule, which is little known and less fixed?” According to *Federalist No. 62*, this little known/less fixed conception of law “poisons the blessings of liberty itself.”

So, aside from the other problematic aspects of the net neutrality rule – the FCC’s acting in the absence of evidence of market failure or consumer harm, the likely adverse economic effects, and the undermining of the agency’s independence – the net neutrality rule also calls into question the FCC’s adherence to fundamental rule of law norms.

Thank you for giving me the opportunity to testify today. I will be pleased to answer any questions.

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<sup>46</sup> Friedrich A. Hayek, *The Road to Serfdom* 80 (1944).

**Statement of Bradford P. Campbell, Esq.  
ERISA Attorney and Former U.S. Assistant Secretary of Labor  
For Employee Benefits**

**Before**

**The U.S. Senate Committee on Homeland Security and Governmental Affairs**

**Hearing on**

**The Administrative State: An Examination of Federal Rulemaking**

**April 20, 2016**

**Introduction:**

Chairman Johnson and Ranking Member Carper, thank you for the opportunity to testify regarding the need to reform the Federal regulatory process.

My testimony today reflects my personal views as a former Federal regulator and as a current ERISA attorney, and not those of any client, of my firm, or of my colleagues. I am not testifying on behalf of any client or any other party.

I commend the Committee for holding this important hearing not just on the alarming growth in Federal rules and regulations, but also on the manner in which Federal rule-making authority is being misused by some Federal agencies.

The sheer scope of Federal regulation is remarkable. What we eat, what we wear, what we drive, how we work, how we save, even the air we breathe—nearly every fundamental activity of our lives is now at least partially subject to Federal regulations. While there is a legitimate role for Federal regulation, it is fair to say that the current regulatory environment—and the practices of some Federal regulators—are in significant need of review and reform.

**Current Regulatory Practices Overstep Intended Scope of Authority:**

Regulatory authority delegated to the Executive Branch by Congress was not intended to make Federal regulators an ersatz legislative body, but to facilitate the practical implementation of laws passed by Congress. The Administrative Procedure Act and related laws, as well as the various Executive Orders and Office of Management and Budget guidance documents governing the regulatory process, are intended to ensure that such rules are promulgated in a manner consistent with the intent and direction of Congress in Federal law, and only after a thorough and fair consideration of the economic impact, costs and alternatives available to achieve these goals.

Unfortunately, the reality of the regulatory process is all too often quite different.

The ambition of some Federal regulators has eclipsed this limited delegation of authority, and we are increasingly seeing regulations that are, in effect, new Federal laws and policies created by unelected officials rather than Congress. These regulators are using the rulemaking process to make policy and legal judgments that are properly the responsibility of Congress—in fact, some regulators are promulgating rules that clearly conflict with the intent of Congress, but which they attempt to justify through aggressive and convoluted interpretations of their delegated authority, knowing that costly litigation or a literal “act of Congress” is the only real brake on their efforts.

Even more common, rather than using economic impact analysis to inform the development of the policy itself, carefully considering and choosing among alternatives as they are required to do, Federal agencies increasingly use the economic analysis as an after-the-fact paperwork exercise seeking to justify the predetermined policy position of the agency.

I believe the recently promulgated final rule by the U.S. Department of Labor governing investment advice related to \$15 trillion in retirement savings is just such an example of a regulation that infringes on Congressional prerogatives, that is contrary to the intent of the legislation it claims to interpret, and that uses the economic analysis to justify its predetermined policy decision, rather than to inform the development of its policy and to consider alternatives.

**Labor Department Fiduciary Rule Highlights Why Reform is Necessary:**

As the former U.S. Assistant Secretary of Labor for Employee Benefits and head of the Employee Benefits Security Administration, I have personal experience with the scope of the Labor Department’s authority, and in exercising that authority to implement the laws passed by Congress. One of my primary duties during my tenure was to promulgate regulations implementing the Pension Protection Act of 2006.

In that law, Congress specifically delegated certain decisions to the agency, including the definition of a Qualified Default Investment Alternative (“QDIA”). This was a significant regulation, as it determined what investments commonly are selected for participants automatically enrolled in 401(k)-type plans, or who otherwise do not provide investment direction for their own accounts. Billions of dollars have been allocated to investment products and services that meet the definition we adopted in the final rule. However, we were exercising authority specifically delegated by Congress to make a particular decision based on extensive discussions with all of those affected by the rule, as well as a thorough public notice and comment rulemaking process. In my view, this is an example of the proper use of regulatory authority.

By contrast, the new fiduciary regulation—which likely is the most sweeping change to retirement savings and financial regulation since the 401(k)—is entirely the product of the Department’s own initiative. The law did not change. If anything, Congressional direction

was for a fiduciary standard to be handled by the Securities and Exchange Commission ("SEC") through a provision of the Dodd-Frank Act.

- **Labor Department Final Rule is Legislation-by-Rulemaking**

Even more concerning, the Labor Department decisions, though described as necessitated by changing circumstances in the retirement marketplace, are contrary to the intent of Congress. Congress did not intend for the Labor Department to become a primary regulator of the conduct and compensation of financial advisors to Individual Retirement Accounts ("IRA"). Congress did not intend for the unique fiduciary standard of care applicable to employee benefit plans under the Employee Retirement Income Security Act of 1974 ("ERISA") to apply to IRAs.

In fact, Congress created ERISA plans and IRAs at the same time, and affirmatively chose NOT to apply the ERISA fiduciary standard to IRAs. The reason is clear—in an ERISA plan, a fiduciary makes many decisions for me, and thus a fiduciary standard rooted in trust law strictly governs those decisions over which I have no control. By contrast, in an IRA, I make my own decisions, so Congress treated IRAs much as it treated other types of investment vehicles, and relied on the extensive network of Federal and state financial regulators and laws already protecting investors. Congress created a new private right of action and legal remedies for ERISA plans, but did not create a special cause of action for IRAs. Rather than create an IRA-only cause of action, Congress let recourse against investment advisors be determined by the Federal and state regulation applicable to the type of advisor.

In other words, Congress made affirmative choices about the different roles of ERISA plans and IRAs, and while they share a common bond in the prohibited transaction rules, they were intended to be regulated quite differently otherwise.

Remarkably enough, these intentional Congressional decisions are exactly the flaws the Labor Department cited to justify its new set of judgments displacing Congressional intent. Regulation is needed, said the Labor Department, because there is no independent fiduciary protecting the IRA owner. The Best Interest Contract (BIC) Exemption right for an IRA owner to bring a class action in state court for breach of contract is needed, said the Labor Department, because there is no separate cause of action for IRAs. Underpinning all of this is the belief by the Labor Department that securities, insurance and other financial laws applicable to IRA advisors generally are inferior to ERISA, and that IRAs should be treated more like ERISA plans, largely because ERISA plan assets are frequently rolled over into IRAs.

To achieve this, the Labor Department took a legal two (or maybe three) step. First, it expanded the definition of what constitutes fiduciary investment advice under ERISA. Then, based on a 1978 reallocation of regulatory authority in the Carter Administration that gave the Labor Department interpretive authority over the prohibited transaction rules in both ERISA and the Tax Code, it applied that new fiduciary definition to the Tax Code prohibited transaction rules. These rules apply to IRAs. Thus, the final regulation turns an advisor to an IRA, whose compensation is entirely consistent with the securities

laws (let's assume the advisor is a registered representative of a broker dealer) into a person committing a prohibited transaction under the Tax Code. The BIC Exemption is now necessary for that registered representative to give advice or to help a participant with a rollover, because the advisor's compensation is causing a prohibited transaction that the BIC Exemption will exempt. The BIC Exemption requires the broker-dealer and the registered representative enter into a contract in which they agree to a fiduciary standard of care based on ERISA, and to be subject to a class action lawsuit in state court if they breach the contract.

In summary, by prohibiting the way certain financial advisors are commonly paid if they give advice regarding ERISA plans, IRAs, rollovers and distributions, and by then offering them a narrow way out through an exemption with conditions, the Labor Department foists onto advisors a standard of care and a legal liability Congress affirmatively chose not to impose.

Whether you think the Labor Department is right that IRAs should be subject to the ERISA standard of care is not the issue. The issue is that this matter is something Congress previously addressed, and changing it should be a Congressional decision, not legislation-by-rulemaking.

- **Labor Department Final Rule Is the Product of a Flawed Process**

Separate from concerns about the Labor Department's authority to issue the regulation given Congressional intent, there are a large number of concerns regarding how the Department promulgated the regulation, and regarding the content of its economic analysis.

In an unusual step, the Office of Advocacy at the Small Business Administration and the Financial Industry Regulatory Authority ("FINRA") both offered formal comments on the public record after the proposed regulation was released. FINRA offered 21 pages of comments identifying various problems, including direct conflicts with securities law and regulation, created by the Proposal.<sup>1</sup> While some of these were addressed in the final rule, not all of them were.

The Small Business Administration's ("SBA") Office of Advocacy expressed concerns in its formal comment letter to the Department, questioning the Department's economic analysis and criticizing the Department for not sufficiently taking into account the effects of the Proposal on small businesses. The conclusion from focus groups held by the SBA was that "the proposed rule would likely increase the [advisers'] costs and burdens associated with serving smaller plans...[and] could limit financial advisers' ability to offer savings and investment advice to clients...ultimately lead[ing] advisors to stop providing retirement services to small businesses."<sup>2</sup>

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<sup>1</sup> See, Comment letter from Financial Industry Regulatory Authority ("FINRA"), July 17, 2015.

<sup>2</sup> Comment letter from the Small Business Administration's Office of Advocacy, July 17, 2015, at 5-6.

Even more significantly, this Committee issued a report detailing the findings of its inquiries with the SEC and other Federal agencies regarding their interaction with DOL. I won't repeat in detail here the findings of the Committee's own report, but it contained remarkable information showing that:

- Treasury Department officials questioned the rule's IRA provisions, and viewed them as contrary to Congressional intent;
- The SEC staff raised many issues that the Labor Department ignored in the proposed regulation; and
- Despite requirements to consider the costs and benefits of alternative approaches, Labor Department staff objected on the grounds that it would be difficult and delay the project.

The Labor Department also persists in using unrealistic assumptions about the costs of implementing the final rule. To highlight just one example, let me address their estimates for the cost of legal advice. The final rule estimates that the average hourly rate of legal advice to assist in compliance with the rule would be about \$134. As an ERISA attorney in private practice, I can assure you that this is an utterly unrealistic estimate. Similarly, in estimating the cost of using attorneys to write required disclosures, the Labor Department estimated that a simple disclosure would take only one attorney 10 minutes to write. As an ERISA attorney I can assure you that a disclosure that could be part of the basis for a class action lawsuit against a financial entity's entire book of business takes far longer than 10 minutes to write, and is reviewed and debated by far more than one attorney. It does not cost \$22.33 to meet that disclosure requirement.

Finally, while the Labor Department makes much of the fact that it offered a lengthy comment period and held public hearings on the rule, it is important to note that all of the comments and hearings were only addressing the proposed rule. Rather than demonstrating an open process, these facts serve to highlight the complexity and ambiguity of the proposal itself. In my experience, it is very unusual for the Labor Department to move to a final rule when literally dozens of major issues regarding a proposal are in dispute. Further, the comments did not present the Labor Department with a binary choice on addressing those issues, but a range of options.

Unfortunately, the Labor Department choose not to provide even a brief comment period on a revised rule, and as a result, the final rule is the first time we have seen how the Department addressed many of these concerns. The dozens of changes are therefore quite surprising. The final rule contains new provisions not even discussed in the proposal, such as making a recommendation as to the type of account a new form of fiduciary advice.

It also makes major changes to the exemptions for new reasons not previously discussed. For example, the proposal removed individual variable annuities from PTE 84-24 (an exemption for annuities and insurance policies) and made only the BIC Exemption available. The rationale then was that such annuities are registered as securities and



therefore should be under the BIC Exemption with most other securities. However, the final exemption removed not just individual variable annuities but also group variable annuities and fixed index annuities from PTE 84-24. The new rationale had nothing to do with status as a security (which the latter two are not), but rather with the Department's apparently new concerns about the marketing of such products.

Given the large number of fundamental and new changes, the Department should have repropose the rule for a brief comment period—instead, it forged ahead, making educated guesses about how to proceed. This is not consistent with the law or the Executive Orders and guidance addressing the process.

**The Big Picture—Regulatory Reform is Needed to Address the Tension between Congressional and Executive Authority:**

The Department of Labor's recent fiduciary regulation offers some valuable lessons in the way in which the rulemaking authority is misused by some agencies, as well as the standards, criteria and review process to which this authority is subjected. The rule illustrates two closely related challenges.

First is the inherent difficulty Congress faces in finding the right balance between providing Executive branch agencies the authority needed to administer complex statutes while retaining its Constitutional authority to legislate. How does such reform facilitate the work the Labor Department did on the QDIA regulation, but prevent the work it has done on the fiduciary rule?

Second is the hazard inherent in maintaining the kind of broad grants of regulatory authority that have typically been incorporated into Federal laws such as ERISA. As I explained above, and as the Committee detailed in its own report, the regulatory authority here was used in a particularly convoluted way to achieve its objective. I believe it went too far, but that will likely be a matter settled in the courts.

The ongoing tension between Congressional and Executive branch authority remains a political and public policy theme that is increasingly at the forefront of political disagreements. The Labor Department's recent actions may well be addressing an issue worthy of public debate, but the agency has done so by contorting the reasonable limits of the reach of its jurisdiction and unilaterally imposing new and costly requirements on a major part of our economy affecting all of us. Exercising necessary interpretive authority in response to changing circumstances and attempting to legislate through the regulatory process are two very different things, and Congress should be mindful of the latitude it has granted to agencies both in the statutes they implement, and in the regulatory process itself.

It is in the gaps and ambiguities of the allocation of regulatory authority that controversial regulations of the sort we are increasingly experiencing take root. Complex statutes like ERISA, with their origins in an earlier era in which Federal agencies played a much smaller role and to which fairly broad authority was granted, are fertile ground for regulatory

overreach. Federal rulemaking at an agency becomes an attractive policy alternative to Congressional action for an Executive Branch facing Congressional opposition to its views.

This is a very worrisome development, because the regulatory process has relatively few checks and balances compared to the legislative process—the authority of the agency to push forward despite criticism and public outcry is relatively unfettered, except to the extent the agency does not follow the proper process or makes a decision this is “arbitrary and capricious” in the view of a Federal court. While public and notice comment rulemaking provides an opportunity for affected persons to make their views known on the record (at least with respect to the proposed regulation), the reality is that the agency is under no obligation to do more than properly consider those comments. Contrast this to a Congressional debate, where a majority must prevail in votes in two separate bodies against active internal opposition, and must then convince the President to agree or must override his veto with a two-thirds majority. At the end of the day, a Federal agency that intends to make policy and that has the will to proceed is very difficult to stop unless Congress takes a stand, or the courts overturn the action after the fact.

**The Fragmented and Not-Easily Enforced Current Regulatory Process Needs Reform:**

- **Fragmented Authority**

The ERISA fiduciary regulations also bring to light the problematic nature of the fragmented and sometimes piecemeal nature of the standards and criteria applicable to the promulgation of regulations. The basic procedural standards governing the process date back to 1946 with the Administrative Procedures Act (APA) and remain essentially the same today. The APA, reflecting the concerns of an earlier era, however, primarily addresses the procedural requirements and transparency of the rulemaking process rather than the scope of authority that is exercised or the quality of the supporting analysis or decision making that underlies a regulation. A variety of new requirements have been added through laws, Executive Orders and operational guidelines beginning in the 1980's, such as requiring that the impacts on small businesses be explicitly measured and considered, that any unfunded mandates on State and Local Governments be addressed, and that the regulatory decisions be undertaken on the basis of an evaluation of costs and benefits, including the use of alternatives that provide the most cost effective solution to a clearly defined need.

- **Difficult to Enforce Requirements**

These requirements, however, are often poorly coordinated and lack an effective mechanism to ensure they are fully complied with by regulatory agencies. Some of these requirements are contained in statutes and provide the basis for a legal challenge in the courts if not fulfilled. Others, especially the standards and criteria for a complete and credible economic impact analysis, are primarily within Executive Orders and Office of Management and Budget (“OMB”) policy guidance, which provide essentially no means for the regulated community and Congress to ensure they are met. Although the Unfunded

Mandates Reform Act of 1995 contains a requirement for regulatory impact analysis to be developed for rules that are likely to result in an expenditure of \$100 million or more by the private sector, it does not specify meaningful standards for the scope or quality of this analysis and provides only for limited judicial review of agency compliance with these requirements. The more in depth and meaningful requirement for regulatory actions to be predicated on and developed on the basis of cost-benefit analysis are established in Executive Order 12866 and the standards for these set forth in OMB Circular A-4. Other related requirements that are in the Federal statutes apply primarily to small businesses.

The absence of a comprehensive set of enforceable standards that governs the quality of regulatory decisions makes it very difficult to hold the regulatory agencies accountable for their actions. Meaningful recourse can typically only be pursued through costly and time consuming litigation. Executive orders and policies often disclaim any private cause of action and thus provide insufficient foundation for success in a legal challenge. Incorporating these various requirements and standards into a single comprehensive law that provides a readily accessible venue to challenge agency actions would go a long way to improving both the quality and accountability of the process.

- **The Role of OMB as Gatekeeper is Conflicted**

The sources of quality control and recourse that currently exist are flawed and inherently weak in the outcomes they produce. The current regulatory review process within the Executive Branch is administered through the Office in Information and Regulatory Affairs ("OIRA") within OMB. While certainly providing some degree of oversight and quality control over "routine" regulations, as well as a venue for affected parties to express their views during the review process, OIRA does not meaningfully protect the public from abuses of the process regarding major regulations because it is part of the Executive Office of the President, which ultimately determines the policies Federal agencies pursue. It cannot, as evidenced by the Labor Department's fiduciary rule, be relied on to impose meaningful standards and control on a regulatory priority that has been identified as a priority by the President to whom it directly reports.

- **Need for Additional Congressional Role**

Of course, Congress can and does provide oversight of the activities of Federal agencies. That is, after all, why we are here today. However, the primary mechanism in the Congressional Review Act has limited utility as a check on regulatory excess. While providing for delayed effective dates to enable some external review and to ensure time for Congress to consider a resolution of disapproval to overturn a regulatory action, such a resolution is subject to a Presidential veto necessitating the requisite two thirds majority to overturn. In the nearly twenty years since the enactment of these provisions, only a single regulation has been overturned through this process. A more robust and accessible form of Congressional review appears to be required to provide more consequential oversight.

### **Other Calls for Reform**

I also want to mention that I serve on the Policy Board of the American Benefits Council (the “Council”)<sup>3</sup> which has been working to review the regulatory process (this review is unrelated to the Labor Department rule). The Council formed a board-level Regulatory Process Task Force in the fall of 2015 and I have had the privilege of chairing that task force. The task force has been working on principles to guide us in reviewing the regulatory process and a draft version of that document is attached as an appendix to this testimony.

The Council has separately developed four relevant principles that I commend to the Committee’s attention.

First, it is very important that the agencies adopt a “least burdensome compliance” standard that fully incorporates technological capabilities in conjunction with all regulations. Before imposing any new administration or reporting requirements, the agencies should be required to “verify they are unable to achieve the objective in a manner less burdensome on the regulated parties...”

Second, regulatory agencies should adopt a “good faith” standard for purposes of enforcement of many regulations. For example, a “good faith” standard would allow employers to use technology as it becomes available, rather than waiting for regulatory approval, where such adoption in good faith serves the requirements of the current regulations.

Third, the agencies should eliminate duplicative, contradictory or excessive regulations that impose administrative burdens on employers. One way to improve the regulatory system would be to emphasize exception-based regulations that target employers with poor performance rather than imposing burdens on all employers. For example, in employee benefits, many regulations are intended to address real or perceived concerns related to small plan sponsors and yet those small plan sponsors often receive an exemption from the resulting regulations.

Fourth, as previous discussed in my background materials, coordination of rules between Congress and the agencies – and across those agencies – should be improved. Employer-sponsored benefit plans are complex entities that are subject to the jurisdiction of different congressional committees and regulatory agencies. When multiple agencies share rulemaking authority on a particular issue, employers must accommodate differing (and sometimes contradictory) obligations. In addition, after important legislation is enacted, employers must comply with the statutory requirements until regulations are issued.

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<sup>3</sup> The American Benefits Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council’s members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

Future legislation should clearly indicate enforceable timing for issuance of enabling regulations and/or make the statutory requirement effective date contingent on the promulgation of the regulations.

**Conclusion:**

Thank you Mr. Chairman and Ranking Member Carper for your commitment to reviewing the Federal regulatory process. I believe this Committee could significantly improve the current situation, protect Congress' Constitutional role, and ensure better and more efficient regulation through comprehensive regulatory reform. I appreciate the opportunity to discuss these issues with the Committee, and I would be happy to answer any questions you may have.



April 2016

**The Guidance Process  
in the Context of the Voluntary Employer-Sponsored Health and  
Retirement Plan System:  
Principles to Guide Us**

The regulatory authority provided to federal agencies, as well as the authority such agencies exercise in issuing sub-regulatory guidance (as defined below), is a source of both comfort and concern to our members. When used properly, interpretive regulatory authority fills in the technical and practical gaps in the law (whether new or established) and facilitates smooth implementation while taking advantage of the input and technical expertise of the regulated community. In other circumstances the exercise of regulatory authority can amount to a unilateral exercise of agency authority without full consideration of the costs and burdens on the regulated community that exceeds the authority delegated to the federal agency or is inconsistent with the applicable guidelines, or worse, a pretext for law-making outside of Congressional direction. Similarly, sub-regulatory guidance can be a useful tool for quickly addressing our members' concerns, or a worrisome source of new policy that is unilaterally imposed without an opportunity for consultation and review.

Recent experience provides examples of both outcomes, indicating the importance of making the process more consistent across the issues and federal agencies that exercise regulatory authority. This document proposes a set of principles tailored to the unique guidance structure applicable to employee benefits that can provide a policy framework that will improve the consistency and effectiveness of the regulatory and interpretive process. These principles are derived from our review of recent actions by federal agencies with the goal of promoting the proper use of the guidance functions.

Any discussion of the guidance process regarding health and retirement plans needs to focus on two critical points. First, the objective of the employer-sponsored health and retirement plan laws is to provide important health care coverage and a secure retirement to the millions of working Americans. Second, the employer-sponsored system of benefits – whether health or retirement – is a voluntary system

(notwithstanding penalties imposed on employers that do not offer health benefits), and employees and the federal government both benefit when it is easier for employers to remain actively engaged in sponsoring health and retirement coverage. Thus, it is especially important that the regulatory process work in a way that minimizes burdens and preserves incentives for employers to maintain plans.

In addition, to ensure that regulatory agencies properly fulfill their role, in these situations, there should be a clear definition of the scope of the authority of Congress, i.e., to legislate, and of the executive branch agencies, i.e., to interpret and administer those laws. In our Constitutional system, executive branch agencies should not attempt to legislate through the interpretive process. Although Congress sometimes directs the development of regulations to flesh out the details of a new rule, regulators must take care not to pursue policy initiatives absent clear direction and a specific grant of authority from the legislature.

In addition to administrative law (the law governing agency rulemaking), these basic principles should underlie any analysis of the guidance process or exercise of administrative authority. This requires that decisions regarding whether and how to regulate be made on the basis of good decision-making principles and sufficient consultation and knowledge and be limited to actions that can demonstrably support the extension, maintenance and security of health and retirement plans. Based on this framework, we have developed a set of principles that should guide the process with respect to the employer-sponsored system. It is our hope that these principles can lead to a robust dialogue regarding how best to improve and enhance the health and retirement systems.

#### SUMMARY

*Economic Analysis Principle: A thorough economic analysis should support any decision to impose new burdens on employers maintaining a health or retirement plan and ensure that it results in the most cost effective outcomes.*

- *Sub-principle #1: Any decision to develop new regulations or impose additional burdens should be supported by economic analysis that indicates the need and demonstrates how the action will achieve a positive outcome by evaluating the full range of direct and indirect impacts.*
- *Sub-principle #2: Consistent with applicable Executive Orders and OMB guidance, the economic analysis should include an analysis of all feasible alternatives to achieve the desired policy result and explain how the proposed action was determined to be the least burdensome means of achieving that result.*

- **Sub-principle #3:** Economic analyses should not examine any new proposed rule in isolation; it is critical that economic analyses consider the regulatory context, including other related rules.

**Notice and Comment Principle:** To the greatest extent that is feasible and in any case where guidance or enforcement would establish new binding standards or impose new requirements or result in a material economic impact, the notice and comment process as set forth in Section 553 of the Administrative Procedures Act (and associated requirement for an economic impact analysis) should be used.

- **Sub-principle #1:** Whenever guidance or enforcement would impose new requirements, the notice and comment process should be used, rather than using sub-regulatory guidance.
- **Sub-principle #2:** When any form of regulatory process is used, the final rules should not include new law, standards or requirements that were not subject to notice and comment.
- **Sub-principle #3:** Whenever sub-regulatory guidance could result in economically significant outcomes, the notice and comment process should be used pursuant to widely overlooked Office of Management and Budget ("OMB") guidance.
- **Sub-principle # 4:** In narrow circumstances, advance notice and comment is not appropriate where an existing rule is causing unintended and immediate harm or where the new guidance will relieve rather than establish new requirements or burdens.

**Treasury Adherence Principle:** Treasury guidance should be subject to the foregoing principles, except in the narrow circumstances contemplated by Congress where rules can be issued without advance notice and comment in order to correct mistakes, prevent inequitable administration of the tax laws, or protect federal revenues. The default process should be the use of notice and comment. Any determination to issue rules without notice and comment should include a justification for why this approach is appropriate.

**Increased Private Sector Interaction Principle:** In addition to the formal notice and comment process, government guidance would benefit from increased interaction between the government and stakeholders with respect to the challenges of implementation, anticipated costs and benefits, and the possibility of indirect or unintended effects.



**Congressional Effective Date Principle:** *The effective date of new statutory restrictions should be based on the publication of administrative guidance. If a statute has a fixed effective date, and, as is often the case, administrative guidance regarding the new restrictions is not issued sufficiently in advance of that effective date, compliance is very difficult. Moreover, in such cases, employers are often forced to restructure their operations once as of the statutory effective date and again as of the effective date of the administrative guidance.*

**Rulemaking Authority Principle:** *When issuing regulations or other administrative guidance, the executive agencies should be careful to ensure their actions are within the grant of specific administrative authority provided by Congress. Agencies should include a complete explanation of how the specific exercise of any regulatory authority falls within their specific remit of authority.*

**Federal Intra-Agency Coordination Principle:** *Employer plans are often made subject to multiple regulatory regimes at the federal and state level. Often these regimes may impose similar, but not identical, requirements. To reduce confusion as well as the complexities and costs associated with complying with multiple regulatory schemes, the federal agencies should work together to fashion a coordinated set of rules or otherwise establish a deeming approach which would allow employers to be deemed in compliance with one scheme by complying with another.*

## DISCUSSION

### Economic analysis

**Principle:** *A thorough economic analysis should support any decision to impose new burdens on employers maintaining a health or retirement plan and ensure that it results in the most cost effective outcomes.*

- **Sub-principle #1:** *Any decision to develop new regulations or impose additional burdens should be supported by economic analysis that indicates the need and demonstrates how the action will achieve a positive outcome by evaluating the full range of direct and indirect impacts.*
  - Too often, an economic analysis is developed to support what appears to be a pre-determined policy decision, rather than determinations that are supported by economic analysis to determine if there is an economic justification for any new rulemaking by either indicating substantial negative economic consequences of the current environment or demonstrable advantages that will accrue from the action.

- Economic analysis, consistent with OMB guidance on implementing the applicable executive orders, should be complete in its scope by considering not just the direct impact of the action but also any indirect or collateral results that can be reasonably be expected to result from the action.
- A thorough analysis should include consultation with experts from the private sector. Early discussions with the private sector can avoid the government pursuing regulatory paths that impose unnecessary costs and will not be effective in improving outcomes.
- In order to gain more understanding of the economic effects of a possible proposal, the government should increase the use of “Requests for Information” prior to the issuance of proposed regulations. This can complement informal outreach to private sector experts in examining the economic effects of a possible proposal and ensure that the threshold decision to undertake a regulatory action is fully justified.
- *Sub-principle #2: Consistent with applicable Executive Orders and OMB guidance, the economic analysis should include an analysis of all feasible alternatives to achieve the desired policy result and explain how the proposed action was determined to be the least burdensome means of achieving that result.*
  - Economic analysis should outline the full range of approaches to achieving a defined policy objective and assess the costs and benefits of all feasible alternatives to demonstrate how the decisions made in developing the rule are the most cost effective. This should be a major focus of the economic analysis and the work described above with private sector experts.
  - Economic analysis should include tailored efforts to target reforms at the situations where reforms are needed. For example, if a regulatory requirement is not necessary for businesses of a certain size (large or small), then appropriate exceptions should be crafted. Similarly, if problematic practices are limited to certain classes of businesses, such as small professional businesses, regulatory requirements should be limited to those classes of businesses, rather than burdening all businesses.
- *Sub-principle #3: Economic analyses should not examine any new proposed rule in isolation; it is critical that economic analyses consider the regulatory context, including other related rules.*

- Employee benefits plans fall within the direct and indirect authority of a wide range of federal agencies including the Departments of Labor, Treasury and health and Human Services and the Pension Benefit Guaranty Corporation which have specific direct regulatory responsibilities as well as a wide range of other agencies that oversee financial services, consumer protections, and a variety of aspects of labor law.
- These disparate agencies often operate within their narrow areas of jurisdiction without adequate consultation with the other agencies that may have overlapping or related authority or fully contemplating the interaction of their rules with the complex web of requirements affecting the operation of employee benefit plans.
- The laws, policies and procedures governing the regulatory process have been developed largely in consideration of agencies with more narrow and focused authority and do not include requirements to fully consider and address the need for consultation and coordination of requirements imposed by different agencies.
- A good example of this problem are the numerous new disclosures and participant communications required by the Affordable Care Act ("ACA") and implementing regulations. The ACA imposes a host of new reporting and disclosure requirements on employers and plans, including the employer exchange notice, advance notice of certain material modifications, expanded reporting of employer-sponsored group coverage, and employer reporting of employee enrollment in minimum essential coverage and employer compliance with the employer "shared responsibility" provisions.
- The economic analyses performed with respect to each of these new disclosure and reporting requirements look solely at the incremental costs/burdens to employers and plans, and fail to take account of the overall costs of creating and furnishing all of these disclosures in the aggregate.
- To engage in such a piecemeal economic analysis understates the overall burdens imposed upon employers by the current spate of disclosure requirements. It is important that future analyses take into consideration not just the new marginal burdens/costs, but the overall effect on employers.

### Notice and comment process

***Principle:** To the greatest extent that is feasible and in any case where guidance or enforcement would establish new binding standards or impose new requirements or result in a material economic impact, the notice and comment process as set forth in Section 553 of the Administrative Procedures Act (and associated requirement for an economic impact analysis) should be used.*

- ***Sub-principle #1:** Whenever guidance or enforcement would impose new requirements, the notice and comment process should be used, rather than using sub-regulatory guidance.*
- ***Sub-principle #2:** When any form of regulatory process is used, the final rules should not include new law, standards or requirements that were not subject to notice and comment.*
- ***Sub-principle #3:** Whenever sub-regulatory guidance could result in economically significant outcomes, the notice and comment process should be used pursuant to widely overlooked Office of Management and Budget (“OMB”) guidance.*
- ***Sub-principle # 4:** In narrow circumstances, advance notice and comment is not appropriate where an existing rule is causing unintended and immediate harm or where the new guidance will relieve rather than establish new requirements or burdens.*
  - The Administrative Procedure Act (“APA”) requires that regulatory guidance establishing substantive new law or standards (what is termed “legislative rule making”) be issued through a process that includes the publication of proposed regulations in the Federal Register, followed by a comment period before the issuance of final regulations. This process is set forth in Section 553 of the APA. An exception to this process is provided for what are termed “interpretive” rules or what is often called “sub-regulatory guidance” where the agency is narrowly interpreting the meaning of a statute rather than establishing substantive law or requirements.
  - In January of 2007 the Office of Management and Budget issued a “Bulletin of Good Guidance Practices” (which ostensibly remains in effect) that establishes a presumption of the need to provide an economic analysis and justification for rules that entail a significant economic effect.
  - Regulatory agencies however are currently afforded broad discretion by OMB in determining which of their actions fall within these categories. This has resulted in circumstances in which rules and regulations of a

substantive nature have been imposed without any notice and comment with the only recourse available to the affected community a costly and time consuming legal challenge in the courts.

- Re-establishing the presumption that rule making activities that establish any new law or requirements should require public consultation through the notice and comment process and that any exceptions to this be made on the basis of a fully articulated justification that is made publically available in advance and approved by OMB would preclude the possibility of agencies imposing costly new requirements without the necessary public consultation.
- An exception to this requirement is appropriate for the expedient provision of regulatory relief in circumstances where an existing rule is causing unintended or immediate harm or where the action of the agencies is to relieve rather than to impose new regulatory burdens. In these circumstances however the regulatory agency should be required to provide the rationale for using such an exception.

#### **Treatment of Treasury guidance**

*Principle: Treasury guidance should be subject to the foregoing principles, except in the narrow circumstances contemplated by Congress where Treasury rules can be issued without advance notice and comment in order to correct mistakes, prevent inequitable administration of the tax laws, or protect federal revenues. The default process should be the use of notice and comment. Any determination to issue rules without notice and comment should include a justification for why this approach is appropriate.*

- Under Section 7805(b)(1)(C) of the Internal Revenue Code, Treasury may issue an immediately effective notice describing the substance of a regulation that will be issued. This allows Treasury to effectively establish immediately effective new rules without advance notice and comment. This authority was intended to allow Treasury to immediately protect federal revenue, correct mistakes, and avoid inequitable administration of the tax laws.
- The authority was never intended to permit Treasury to set new social policy through the Code. Yet this is exactly what Treasury has done in several recent actions that imposed new restrictions on pension funds ability to offer lump sum payments to retirees already receiving benefits and in other actions that establish requirements under the Affordable care Act (ACA).

- The default position should be that Treasury is required to justify its rules with an economic analysis. The relevant Executive Orders and OMB guidance establishing the requirement for an economic impact analysis do not specifically exempt Treasury. However, in practice, Treasury does not issue analyses of the economic effects of its guidance.
- To the extent that Treasury is simply administering the tax laws and collecting revenue it may make sense that Treasury would not be required to provide an economic impact analysis providing a rationale for its decisions or need to quantify the economic effects of its guidance. However, in the retirement and health benefits areas, Treasury is not simply administering the tax laws; on the contrary, it is making retirement and health care policy. In situations where Treasury is trying to achieve policy objectives wholly separate from collecting revenue, there is no justification for exempting Treasury from the rules requiring advance economic analyses.
- If Treasury makes a decision to issue regulatory guidance under this statutory exception it should be required to provide an explanation and rationale for its determination in conjunction with the guidance that is subject to OMB review and concurrence with its determination to ensure that the exception is used only where appropriate rather than for purposes of expediency and to ensure that there is the maximum feasible transparency and public consultation on rule making with a material impact on the regulated community.

#### **Increased private-sector interaction in the guidance process**

*Principle: In addition to the formal notice and comment process, government guidance would benefit from increased interaction between the government and stakeholders with respect to the challenges of implementation, anticipated costs and benefits, and the possibility of indirect or unintended effects.*

- The structured notice and comment process stipulated by the APA is often undertaken at a later stage in the rule making process after the agencies have already made a decision to promulgate a rule or have formulated a proposal.
- The process is of limited value in these circumstances because the agencies may have based their determinations on an incomplete or inaccurate

understanding of the operations of the affected entities or have not considered the full range of potential alternatives.

- While there is a requirement under current law for the agencies to publish a semi-annual agenda of rule-making actions this has often devolved into a pro forma exercise in which initiatives remain on the list for many years without any meaningful activity or appear just prior to the issuance of a proposal. There are only limited requirements for regular and meaningful consultation with the regulated community and in some cases perceptions of limitations imposed by the APA on communications.
- Treasury publishes a guidance agenda that includes upcoming sub-regulatory guidance. This is extremely helpful in generating more interaction with the private sector. It would be helpful if other agencies could do this too, so that the private sector can provide input in advance.
- The agencies do on occasion issue a formal Request for Information (RFI) as they contemplate future regulatory action which provides an opportunity for the provision of information. However, this process does not afford much opportunity for interactive communications.
- Consideration should be given to encouraging the broader use of the RFI process and potentially requiring it for significant initiatives when feasible.

#### **Congressional effective dates**

***Principle:** The effective date of new statutory restrictions should be based on the publication of administrative guidance. If a statute has a fixed effective date, and, as is often the case, administrative guidance regarding the new restrictions is not issued sufficiently in advance of that effective date, compliance is very difficult. Moreover, in such cases, employers are often forced to restructure their operations once as of the statutory effective date and again as of the effective date of the administrative guidance.*

- Frequently, administrative guidance is not published by the time that new statutory restrictions take effect. This means that the restrictions must be implemented without guidance. Even more troubling, this also means that plan operations may need to be restructured twice, once to comply with the statute and again later to comply with administrative guidance.

- There are several examples with respect to departmental actions regarding the implementation of the ACA where they expressly delayed the application of a new statutory rule until after the issuance of administrative guidance. This approach should be required and be afforded an exception to any APA requirements that may impede the delay of effective dates to allow required guidance to be completed. to ensure that agencies have time to engage in a careful and deliberate public rulemaking process.

#### **Adhering to congressional grant of rulemaking authority**

*Principle: When implementing regulations or other administrative guidance, the executive agencies should be careful to ensure their actions are within the specific grant of authority provided by Congress. Agencies should include a complete explanation of how the specific exercise of any regulatory authority falls within their specific remit of authority.*

- There have been several instances where one executive agency has engaged in rulemaking that goes beyond its Congressional grant of authority. Such rulemaking should be avoided for several reasons. First, it is contrary to general Federalism principles. Second, it has the potential to result in confusion for the regulated community, including the scope of the application of the proposed rule. Third, there is an increased chance that stakeholders may not engage in full and meaningful comment with respect to a proposed rule if they are unaware that the agency intends for the new rule to apply to the stakeholders or their plans. Accordingly, any final rule may suffer from less than robust notice and comment and may not reflect best policy.

#### **Need for greater federal intra-agency coordination to minimize adverse effects of multiple regulatory schemes to employer-sponsored plans**

*Principle: Employer plans are often made subject to multiple regulatory regimes at the federal and state level. Often these regimes may impose similar, but not identical, requirements. To reduce confusion as well as the complexities and costs associated with complying with multiple regulatory schemes, the federal agencies should work together to fashion a coordinated set of rules or otherwise establish a deeming approach which would allow employers to be deemed in compliance with one scheme by complying with another.*

- One good example are employer-sponsored wellness programs, which are subject to a multitude of federal regulations administered by agencies with both direct and indirect authority over employee benefit



plans including the Departments of Labor, Treasury, HHS and the EEOC. While several federal agencies worked together in the context of one of the applicable federal statutes, HIPAA, to fashion tri-agency regulations, wellness programs remained subject to significant regulatory and litigation risk with respect to the ADA administered by the EEOC whose proposed ADA regulations do not fully align the tri-agency regulations.

- In the retirement area, a very recent example of a lack of coordination is the proposed DOL regulation giving states the ability to mandate payroll deduction IRAs. DOL did not place any meaningful constraints on state powers, so that the result may be a patchwork of different rules for national employers operating in many states. In fact, DOL's proposal is so open-ended that it is very possible that multi-state employers could be subject to conflicting rules established by different states with respect to the same employees.
- Where possible, agencies should try to borrow from existing regulatory schemes rather than apply new and different rules to employer-sponsored plans. Otherwise, the effect is to increase the costs and burdens of plan sponsorship/maintenance within the framework of what is otherwise a voluntary system.
- There should be a more formal requirement for consultation and coordination among the agencies and in the materials promulgating any new requirements the manner in which it has been coordinated



## **Statement of the U.S. Chamber of Commerce**

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**ON: Hearing on The Administrative State: An Examination of  
Federal Rulemaking**

**TO: U.S. Senate Committee on Homeland Security &  
Governmental Affairs**

**DATE: April 20, 2016**

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1615 H Street NW | Washington, DC | 20062

The Chamber's mission is to advance human progress through an economic,  
political and social system based on individual freedom,  
incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations. The Chamber is dedicated to promoting, protecting, and defending America's free enterprise system.

More than 96% of Chamber member companies have fewer than 100 employees, and many of the nation's largest companies are also active members. We are therefore cognizant not only of the challenges facing smaller businesses, but also those facing the business community at large.

Besides representing a cross-section of the American business community with respect to the number of employees, major classifications of American business—e.g., manufacturing, retailing, services, construction, wholesalers, and finance—are represented. The Chamber has membership in all 50 states.

The Chamber's international reach is substantial as well. We believe that global interdependence provides opportunities, not threats. In addition to the American Chambers of Commerce abroad, an increasing number of our members engage in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

**BEFORE THE COMMITTEE ON HOMELAND SECURITY & GOVERNMENTAL  
AFFAIRS OF THE U.S. SENATE**

**Hearing on The Administrative State: An Examination of Federal Rulemaking**

**Testimony of William L. Kovacs  
Senior Vice President, Environment, Technology & Regulatory Affairs  
U.S. Chamber of Commerce**

**April 20, 2016**

Good morning, Chairman Johnson, Ranking Member Carper, and distinguished Members of the Committee. My name is William L. Kovacs and I am senior vice president for Environment, Technology and Regulatory Affairs at the U.S. Chamber of Commerce. I was asked to discuss the Chamber's perspective on the current condition of our regulatory state.<sup>1</sup>

The goal of the regulatory process should be to produce regulations that implement the intent of Congress in the most efficient way possible. Accountability, transparency and integrity are the essential characteristics needed to achieve the development of good regulations. Considering that agencies utilizing a "New Deal" regulatory process have issued almost 200,000 regulations between 1976 and today, the regulatory process has generally worked well in managing routine matters. Unfortunately, however, the system is not working as Congress intended for the most complex and high-cost regulations that have the most profound effect on the fabric of our society. Congress needs to pay far more attention to how agencies develop these critical rules since they govern major segments of the nation's activities.

The Chamber has spent several years examining the regulatory process in detail.<sup>2</sup> Our research indicates that, over time, Congress has enacted many broad and vague laws that

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<sup>1</sup> Nothing in these comments shall constitute a waiver of any arguments the Chamber has made or will make in the context of any litigation involving the EPA and Army Corps of Engineers' definition of "Waters of the United States."

<sup>2</sup> See U.S. Chamber of Commerce, *Truth in Regulating: Restoring Transparency to EPA Rulemaking* (Apr. 2015) available at [https://www.uschamber.com/sites/default/files/021935\\_truthinregulating\\_opt.pdf](https://www.uschamber.com/sites/default/files/021935_truthinregulating_opt.pdf); U.S. Chamber of Commerce, *Charting Federal Costs and Benefits* (Aug. 2014) available at [https://www.uschamber.com/sites/default/files/021615\\_fed\\_regs\\_costs\\_benefits\\_2014reportrevise\\_jrp\\_fin\\_1.pdf](https://www.uschamber.com/sites/default/files/021615_fed_regs_costs_benefits_2014reportrevise_jrp_fin_1.pdf); U.S. Chamber of Commerce, *Sue and Settle: Regulating Behind Closed Doors* (May 2013) available at <https://www.uschamber.com/sites/default/files/documents/files/SUEANDSETTLEREPORT-Final.pdf>; U.S. Chamber of Commerce, *Impacts of Regulations on Employment: Examining EPA's Oft-Repeated Claims that Regulations Create Jobs* (Feb. 2013) available at

delegated significant policy making authority to agencies. As agencies began expanding their policy making power, Congress responded by enacting statutes requiring the agencies to analyze, as part of the rulemaking process, regulatory costs and benefits; unfunded mandates; the use of the best quality information, data and peer reviewed materials; impacts on small business and small local governments; as well as mandating, for at least one agency, the continuous evaluation of the potential loss or shifts in employment due to the agency's regulations. These analyses are intended to be a check on agency actions, but as demonstrated below, they are often ignored, to the great detriment of citizens, businesses and state and local governments.

One agency in particular, the Environmental Protection Agency (EPA), has fallen down in its evaluation of critical impact analyses, and at the same time has expanded its regulatory footprint exponentially. Within a period of less than six months in 2015, EPA finalized three massive regulatory programs the Waters of the United States (WOTUS) definition rule<sup>3</sup>, greenhouse gas rules for existing power plants under the Clean Power Plan<sup>4</sup>, and the revised Ozone National Ambient Air Quality Standards (NAAQS).<sup>5</sup> Together, these programs push the boundaries of federal authority further than they have ever been extended. Each of these regulatory initiatives seeks to greatly expand federal power at the expense of state and local governments—despite the fact that the states have long shouldered the vast majority of the burden of implementing and enforcing federal environmental laws, and the ultimate success of EPA's programs overwhelmingly depends on the states.<sup>6</sup> These rules not only undermine the cooperative federalism model carefully crafted by Congress, they threaten to wreak havoc on the ability of states' to operate effective environmental programs.

It is worthwhile to ask – how could this happen? How can federal agencies exercise authority to create laws broader than Congress could enact in a divided government?

The short answer is that for the most costly, burdensome and complex regulations being issued by agencies, the regulatory process is critically dysfunctional. As a result, agencies make more law than Congress, all the while ignoring the impact analyses that Congress requires. Meanwhile, the courts too frequently avoid dealing with the complexity by deferring to agency decisions. And Congress has focused so intently on the problems with specific rules that it has

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[https://www.uschamber.com/sites/default/files/documents/files/020360\\_ETRA\\_Briefing\\_NERA\\_Study\\_final.pdf](https://www.uschamber.com/sites/default/files/documents/files/020360_ETRA_Briefing_NERA_Study_final.pdf); U.S. Chamber of Commerce, *EPA's New Regulatory Front: Regional Haze and the Takeover of State Programs* (July 2012) available at

[https://www.uschamber.com/sites/default/files/documents/files/1207\\_ETRA\\_HazeReport\\_lr\\_0.pdf](https://www.uschamber.com/sites/default/files/documents/files/1207_ETRA_HazeReport_lr_0.pdf); U.S. Chamber of Commerce, *Project No Project, Progress Denied: A Study on the Potential Economic Impact of Permitting Challenges Facing Proposed Energy Projects* (Mar. 2011) available at [http://www.projectnoproject.com/wp-content/uploads/2011/03/PNP\\_EconomicStudy.pdf](http://www.projectnoproject.com/wp-content/uploads/2011/03/PNP_EconomicStudy.pdf).

<sup>3</sup> EPA and U.S. Army Corps of Engineers, "Definition of "Waters of the United States," Final Rule, 80 Fed. Reg. 37,054 (June 29, 2015).

<sup>4</sup> EPA, "Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units," Final Rule, 80 Fed. Reg. 64,662 (October 23, 2015).

<sup>5</sup> EPA, "National Ambient Air Quality Standard for Ozone," Final Rule, 80 Fed. Reg. 65,292 (October 26, 2015).

<sup>6</sup> Testimony of Teresa Marks, Director, Arkansas Department of Environmental Quality and President, Environmental Council of the States, before the House Energy and Commerce Committee, Subcommittee on Environment and the Economy (February 15, 2013) at 3, available at <http://docs.house.gov/meetings/IF/IF18/20130215/100242/HHRG-113-IF18-Wstate-MarksT-20130215.pdf>.

ignored for almost seventy years one of the most important aspects of our complex society—that while regulators make many laws, all legislative power is still vested in Congress and Congress needs to better ensure that agencies carry out its intent. While some members of Congress may be pleased by specific agency action and others displeased, the administrative process has become about how unelected officials make laws. That process must be carried out with accountability, transparency and integrity if it is to provide the management of government the American people deserve.

Reversing this dysfunctional situation is essential to protecting the integrity of Congress as it delegates authority to agencies, but most importantly, to ensure that Congress preserves constitutional checks and balances.

## I. BACKGROUND

A complex society needs regulations; however, as federal agencies regulate more and more facets of American society, they must operate in an even-handed fashion, be open with the public, and follow the directives of Congress.

Preserving transparency and the ability of Congress to manage federal agencies has been a continuing challenge since the day the first regulatory agency, the Interstate Commerce Commission, was created in 1887. Prior to 1935 and the creation of the *Federal Register*,<sup>7</sup> every agency published its own new regulations and there was no central repository for interested parties to monitor. Moreover, agencies were not required to take public comment on their proposed rules and respond to those comments in the rulemaking record until 1946, when Congress enacted the landmark Administrative Procedure Act (APA). The APA established a uniform rulemaking process, citizen participation, procedural transparency, and standards for judicial challenges to agency rulemaking actions.

### A. The Administrative Procedure Act and Rulemakings

Enacted in the wake of the New Deal's vast expansion of federal authority and the government's assumption of extensive control over the U.S. economy in order to fight World War II, the APA was called "the bill of rights for the new regulatory state."<sup>8</sup> One commenter has noted that the APA expressed the nation's decision in 1946 to "permit extensive government, but to restrain agencies' unfettered exercise of their regulatory powers."<sup>9</sup>

The APA was written as a compromise that allows agencies to use informal "notice and comment rulemaking," which means an agency only has to publish a notice of a proposed rule, allow some opportunity for public comment, and respond to any public comments when the agency finalizes the rule. Case law interpreting the APA has established a high bar to invalidate agency action, and courts frequently defer to agencies' technical expertise. The APA's

<sup>7</sup> Federal Register Act of 1935, 44 U.S.C. Chapter 15. The first *Federal Register* notice was published on March 14, 1936.

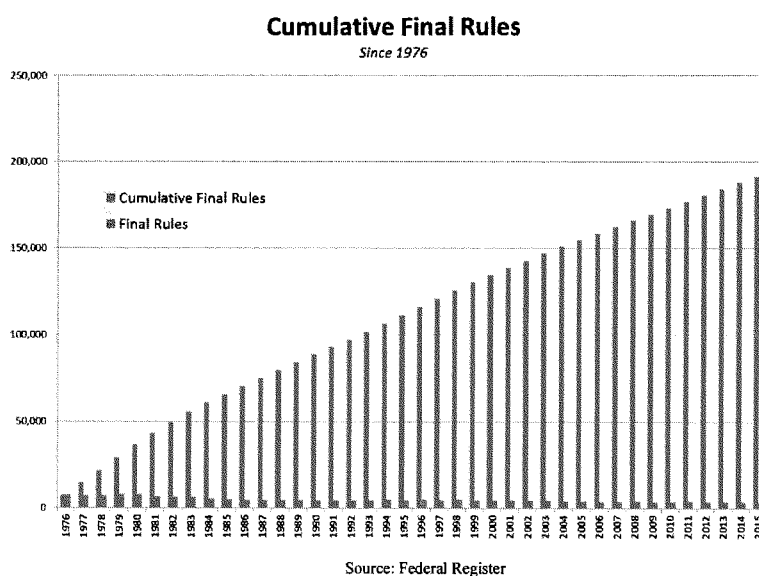
<sup>8</sup> Shepherd, G., *Fierce Compromise: The Administrative Procedure Act Emerges From New Deal Politics*, 90 *Northwestern University Law Review* 1557, 1558 (1996).

<sup>9</sup> See *id.* at 1559.

compromise “struck between promoting individuals’ rights and maintaining agencies’ policy-making flexibility,”<sup>10</sup> actually makes it relatively easy for agencies to issue new rules that, more often than not, will be upheld by the courts.<sup>11</sup>

Each year, federal agencies churn out thousands of new regulations (see Figure 1). For the vast majority of these rulemakings, the APA process has worked very well. Most of the thousands of small rules that agencies propose each year receive little or no public comment and require no procedural effort beyond publishing notices in the *Federal Register*. The ease with which agencies can write new rules helps explain how agencies could collectively issue almost 200,000 final rules over a 40-year period, as illustrated below.

**Figure 1:**



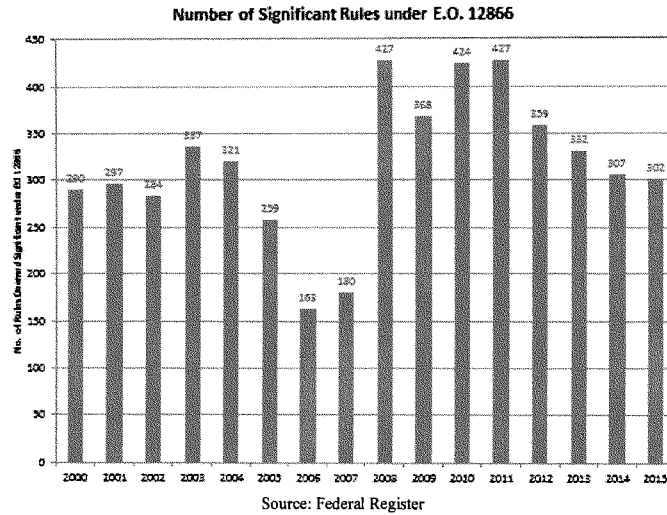
Despite the historic success of the APA in managing small, “run-of-the-mill” rulemakings, the ordinary notice-and-comment rulemaking process has become less and less capable of handling today’s most extensive and costly regulatory actions, which include “significant rules” over \$100 million in cost annually and “high-impact” over \$1 billion annually. Hundreds of significant rules are issued each year (see Figure 2). Of all the significant

<sup>10</sup> *Id.* at 1558.

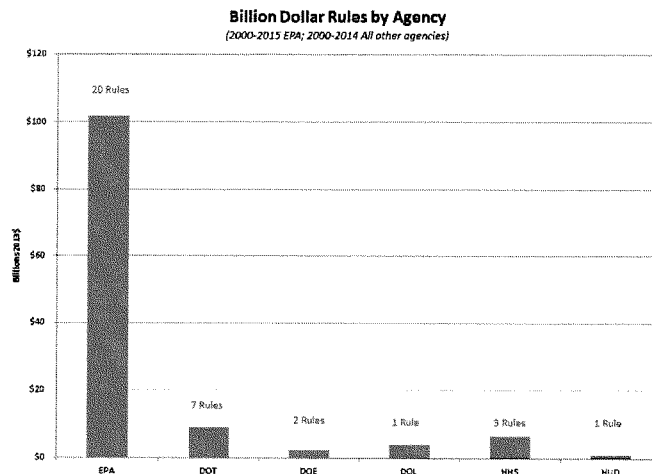
<sup>11</sup> See, e.g., Joseph M. Feller, *Have Judges Gone Wild? Plaintiff’s Choices and Success Rates in Litigation Against Federal Agencies*, 44 ENV’T L. 287, 295 (2014) (citing to studies finding up to 76.6% rates of affirmances by courts in administrative law cases in 1984-85.).

rules issued each year, as shown below, only 34 rules impose **\$1 billion or more** between 2000 and 2015 in regulatory costs.

**Figure 2:**



**Figure 3:**



Sources: EPA rules from agency RIAs; other agencies' rules from OMB 2013, 2014, and 2015, *Reports to Congress on Costs and Benefits of Regulations*.



The data shows that from 2000 to 2015, a total of **34** rules from Executive Branch agencies, each with a cost of more than **\$1 billion** per year, are now imposing nearly **\$125 billion** each year on the U.S. economy.<sup>12</sup> Significantly, EPA not only issued more of these rules than all the other agencies combined, the 20 EPA rules collectively imposed **82%** of all the monetized compliance costs (see Figure 3). While the high cost of these rules is important, these rules are typically also highly complex and burdensome. Such rules are far more intrusive than “run of the mill” rules and have the potential to have profound effects (often unintentional) on fundamental sectors of our national economy (e.g., energy, financial institutions, healthcare, education, and the Internet).

#### **B. The APA Notice and Comment Process Does Not Work For Billion-Dollar-Plus Rulemakings**

One might assume that, because of their importance, agencies would proceed especially carefully when they prepare rules that cost a billion dollars per year or more. In those circumstances, an agency would be expected to analyze and understand how a massive new rule will affect specific regulated industries and the communities where those industries are located. Indeed, as the D.C. Circuit Court of Appeals has noted, the essential purpose of informal notice and comment rulemaking procedures is “(1) to ensure that the agency regulations are tested via exposure to diverse public comment, (2) to ensure fairness to affected parties, and (3) to give affected parties an opportunity to develop evidence in the record to support their objections to the rule and thereby enhance the quality of judicial review.”

Unfortunately, however, agencies often fail to achieve these important objectives, even for billion-dollar-plus rules.<sup>13</sup> Time and time again, informal notice-and-comment rulemaking procedures have proven insufficient to afford interested parties and the public adequate information about the most significant, complex, and costly proposed rules, or adequate time to give useful feedback to the agency in question.

For the most costly and important new rules, informal rulemaking procedures are simply not adequate because of the following factors:

- **Agencies make unproven factual assumptions.** Recent rulemakings have been grounded entirely on assumptions that are speculative and highly likely to be false (e.g., 65% of ozone emission reductions, according to data from EPA’s own Regulatory Impact Analysis for its 2015 Ozone NAAQS rule, are estimated to come from unknown controls that the agency simply assumes will cost the same as existing control technologies<sup>14</sup>).

<sup>12</sup> Independent regulatory agencies (e.g. the Federal Communications Commission (FCC), Securities and Exchange Commission (SEC), and Commodities Futures Trading Commission (CFTC)) are not subject to Executive branch oversight by the Office of Management and Budget (OMB) and do not routinely perform regulatory impact analysis (RIAs) as directed by OMB Circular A-4 guidance on cost-benefit analysis. Consequently, even in the cases when independent regulatory agencies estimate the costs and benefits of their regulations, they generally do not adhere to the standards established and enforced by OMB and the cost estimates are often not complete or comparable.

<sup>13</sup> *International Union, United Mine Workers of America v. Mine Safety & Health Admin.*, 407 F.3d 1250, 1259 (D.C. Cir. 2005), citing *Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 547 (D.C. Cir. 1983).

<sup>14</sup> NERA Economic Consulting, “Economic Impacts of a 65 ppb National Ambient Air Quality Standard for Ozone,” February 2015, available at [www.nam.org/ozone](http://www.nam.org/ozone). (Study and estimates based on data from the EPA’s

The informal notice-and-comment rulemaking process gives stakeholders virtually no real opportunity to disprove these assumptions, because agencies only have to show that they have considered an adverse comment and are essentially free to disregard it.

- ***The public (and very often the agency itself) does not have enough information to fully understand how a rule will work in real life.*** Federal agencies frequently fail to grasp the impact that a large new regulation – added to prior rules and those of *other agencies* – have on businesses, communities, and the economy as a whole.
- ***30-, 60-, or 90-day comment periods are too short to allow stakeholders to develop detailed comments about complex or opaque proposed rules.*** Agencies often take years and sometimes decades to develop large and complex rules and the technical justification. But the public and affected stakeholders are given a far more limited amount of time to evaluate all of the information and data the agency relied upon. By the time a full analysis of a rule’s impact can be completed, the rule is final and has already taken effect.
- ***The information agencies rely upon is often of poor quality, or is not verifiable.*** Agencies often rely on data that is difficult to obtain or verify independently, that is based on too few data points, or was developed using improper methodology.
- ***Agencies are required by law to consider the impacts a new rule will have on regulated entities,<sup>15</sup> but these reviews are limited, rushed, or ignored altogether.*** Agencies have to take shortcuts to meet tight rulemaking deadlines, and often do not complete the analyses necessary to develop a rule that accomplishes its purpose without inflicting unnecessary harm.

## II. A CASE STUDY ON REGULATORY DYSFUNCTION: THE “WATERS OF THE UNITED STATES RULE”

The revised definition of “Waters of the United States” (WOTUS) issued jointly by the EPA and the U.S. Army Corps of Engineers (Corps) on June 29, 2015,<sup>16</sup> expands federal Clean Water Act jurisdiction far beyond the limits explicitly established by Congress and affirmed by the courts. The rule gives EPA and the Corps unprecedented permitting and enforcement authority over land use decisions that Congress intentionally reserved to the States.

The WOTUS rule is a critical example of the type of regulatory mess that results when agencies fail to comply with Congressional mandates. This section details many of the

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Regulatory Impact Analysis of the Proposed Revision to the National Ambient Air Quality Standards for Ground-Level Ozone, pp. ES-8, ES-9 (November 2014)).

<sup>15</sup> See, e.g., Executive Order 12,866 (1993) (requiring interagency economic review of “major rules” that are likely to have an annual effect on the U.S. economy of \$100 million or more); Regulatory Flexibility Act, 5 U.S.C. § 601, *et seq.* (requiring federal agencies to consider the impact their proposed rules will have on small businesses and small governments). Independent agencies such as FCC, SEC, CFTC, and OCC are not bound by this Executive Order.

<sup>16</sup> 80 Fed. Reg. 37,054 (June 29, 2015).

fundamental problems with the WOTUS rule. The agency's procedural failures are detailed in later sections.

### 1. The WOTUS Rule Greatly Expands Federal Jurisdiction Through Complex Definitions.

The rule contains several key new definitions. These new definitions, while important by themselves, also fundamentally transform other existing Clean Water Act definitions. Besides being extremely difficult to fully understand, the interplay of these new and existing definitions has the potential to fundamentally change the relationship between the federal government and the states—all in the absence of any new Congressional directive. Importantly, the WOTUS Rule actually fails to define two critical terms used throughout the rule: “waters” and “dry land”. The final rule preamble lists several types of features that are “waters” but then inexplicably states that features will be “identifiable by water...”<sup>17</sup> The second undefined term is “dry land” – which is used throughout the rule to describe certain types of features, mostly those intended to be excluded from the rule. The agencies concluded that “there was no agreed upon definition given geographic and regional variability”.<sup>18</sup> Considering the complex terms the agency chose to define, it is quite telling that they were unable to define what is water and what is dry land. The new key definitions the agencies decided to include are:

- **“Significant nexus”** - The final WOTUS rule states that any chemical, physical, or biological effect on jurisdictional waters not thought to be “speculative or insubstantial” will be considered “significant.” This so-called “significant” effect can be caused by a single water or wetland or “in combination with other similarly situated waters in the region.” The practical result of the Agencies’ approach is that, if **any** effect exists, it is deemed significant. Moreover, a land user will need to consider not only the effect of the water or wetland on his property, but also the combined effects of other “similarly situated” waters throughout an entire watershed to determine if a nexus exists.<sup>19</sup> This expansion of federal authority is totally unjustified. The concept of a “significant nexus” historically arose in the narrow context of *wetlands* areas that actually abutted—and were therefore “inseparably bound up with”—traditional navigable waters.<sup>20</sup> Now, the WOTUS rule requires an esoteric inquiry into whether an isolated water or wetland could – on its own or in combination with other similar waters -- theoretically have an impact on (or be impacted by) any other water within an entire watershed of a traditional navigable water, interstate water or territorial sea. The meaning of “significant nexus” in the context of chemical, physical, and biological effects could occupy the federal courts for years to come.
- **“Tributary”** - The Agencies’ definition of “tributary” is extraordinarily vague and overbroad. A “tributary” need only demonstrate the bare minimum evidence (including

<sup>17</sup> 80 Fed. Reg. 37055 fn 1 (June 29, 2015).

<sup>18</sup> *Id.* at 37099

<sup>19</sup> The final rule provides a vague and unhelpful explanation of what it means to be “similarly situated”: “waters are similarly situated when they function alike and are sufficiently close to function together in affecting downstream waters.” 80 Fed. Reg. 37,108 (June 29, 2015).

<sup>20</sup> *Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers*, 531 U.S. 159 at 172 (2001) (quoting *U.S. v. Riverside Bayview Homes, Inc.*, 474 U.S. 121 (1985)).

computer-generated evidence, irrespective of actual field conditions) of a water's flow through any channel, a bed, bank and ordinary high water mark. A tributary can be anything that "contributes" even the tiniest amount of water during rare, extreme precipitation events. A tributary may contribute water to major waters by an "indirect" route through another "water," which in turn also could convey only small, infrequent flows via indirect routes. A ditch could be a tributary, if it includes areas that can be characterized as "wetland" anywhere along its entire length, or if they occasionally receive stormwater overflow from any "wetland" or other water. Projects with any land disturbance that includes a ditch are much more likely to trigger a "dredge and fill" permit, and specifically an individual permit instead of a Nationwide permit under section 404 of the Clean Water Act (CWA). Businesses will have to incur the cost and project delays of many more of these permits—which EPA itself has estimated to have a median cost of \$155,000.<sup>21</sup>

- **"Adjacent Waters"** – The application of the term "adjacent" has historically only been used to bring wetlands under federal jurisdiction; however, the final WOTUS rule significantly expands the application of the term to bring "adjacent waters" under federal jurisdiction. The term "adjacent waters" also creates a new term – "neighboring" – which is lengthy, expansive and problematic in its own right. These definitions not only expand the universe of jurisdictional waters far beyond the traditional concept of "adjacency" (and the Supreme Court's interpretation of that concept), they create profound uncertainty as to which waters are likely to be jurisdictional.<sup>22</sup>

Together, these definitions not only expand CWA jurisdiction well beyond anything Congress could have intended to include in the term "navigable waters," but they leave land users with virtually no way to assess the status of their local water, short of undertaking a complex and costly watershed study. A facility may find itself in WOTUS for the first time because it is "adjacent" to or "neighboring" a water, has one or more ditches that are a "tributary," or contains a water that somehow has combined "significant" effects with other "similarly situated" waters to create a nexus.

Very often, the new definitions will create federal Clean Water Act jurisdiction over a vast geographic area previously regulated by the states. The extraordinarily broad scope inhibits the ability of a land owner to make any reasonable judgment concerning the jurisdictional status of any specific, local water. Moreover, by considering a particular water "in combination with" other waters located in such a broad region, the Agencies would examine the cumulative impacts of multiple waters, ranging from large to very small, in order to determine the jurisdictional status of a particular water in question.

<sup>21</sup> EPA and U.S. Army Corps of Engineers, *Economic Analysis of EPA-Army Clean Water Rule* (May 2015), [http://www.usace.army.mil/Portals/2/docs/civilworks/regulatory/news/final\\_CWR\\_eco\\_analysis.pdf](http://www.usace.army.mil/Portals/2/docs/civilworks/regulatory/news/final_CWR_eco_analysis.pdf).

<sup>22</sup> *U.S. v. Riverside Bayview Homes, Inc.*, 474 U.S. 121 at 135 (1985).

## 2. The WOTUS Rule Imposes Massive New Burdens on the States and the Business Community.

Significantly, **EPA itself** developed detailed maps during the WOTUS rulemaking that indicate vastly expanded areas of federal Clean Water Act jurisdiction. These detailed maps, developed by EPA and the U.S. Geological Survey, were released to the public by the House Science Committee on August 27, 2014.<sup>23</sup> The maps indicated more than **8.1 million miles** of rivers and streams across the 50 states could be included under the proposed WOTUS definition.<sup>24</sup> This sharply contrasts with a January 2009 EPA report to Congress that estimated **3.5 million miles** of rivers and streams categorized as WOTUS.<sup>25</sup> Although the final WOTUS rule differs somewhat from the agencies' original proposal, the signification overreach of jurisdiction in the final rule remains.

Based on these EPA maps, the WOTUS rule represents a potential expansion in federally jurisdictional stream miles of at least **130%**. Critical to this analysis, and as discussed further below, EPA certified that the WOTUS rule had no significant impact under the Regulatory Flexibility Act since the rule actually narrowed the scope of waters covered and no small entities are made subject to any new requirements under the definitional changes. It is disingenuous and simply not credible for EPA on the one hand to generate maps demonstrating significant increases in federal jurisdiction, and on the other hand to certify that the rule actually narrows the scope of federal jurisdiction.

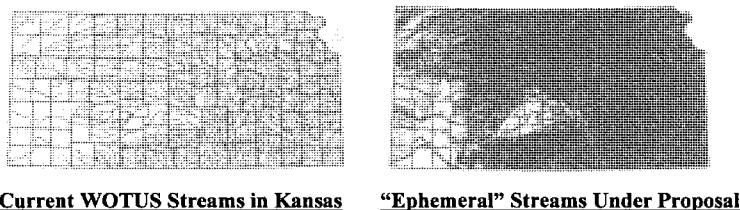
Likewise, analyses by the states of their own waters reveals that the revised definition would increase the amount of stream miles under federal jurisdiction by orders of magnitude. For example, the state of Kansas has estimated that the proposed rule definition of "tributary" would increase the amount of jurisdictional stream miles from around 30,000 miles to 174,000 miles, as shown below, an increase of approximately **460%**.<sup>26</sup>

<sup>23</sup> Press Release, House Committee on Science, Space & Technology, "Smith: Maps Show EPA Land Grab" (August 27, 2014) (the map hyperlink is embedded in the release).

<sup>24</sup> EPA and the Corps consider these revised maps to be good indicators of the extent of federal jurisdiction. The agencies noted that "[w]hen considering whether the tributary being evaluated eventually flows to [a navigable] water, the tributary connection may be traced using direct observation or U.S. Geological Survey maps, aerial photography or other reliable remote sensing information, or other appropriate information." 79 Fed. Reg. 22,202 (April 21, 2014) (emphasis added).

<sup>25</sup> EPA Office of Water, National Water Quality Inventory: Report to Congress, EPA 841-R-08-001 (January 2009).

<sup>26</sup> *Senate Legislative Hearing on S. 1140, The Federal Water Quality Protection Act Before the S. Comm. on Environment and Public Works*, 114<sup>th</sup> Cong. (May 19, 2015) (Statement of Susan Metzger, Assistant Secretary, Kansas Department of Agriculture) ("Currently, in what's approved by EPA as our waters of the U.S. in the absence of the proposed rule, is what we consider those waters with designated uses that are by state statute put into our state surface water quality standards, and that encompasses about 30,000 — a little better than 30,000 — stream miles in Kansas. As we interpret the blanket definition of "tributary" in the proposed rule, that would result in about 174,000 stream miles. That's a 460% increase.").

**Figure 4:**

The expanded jurisdictional areas depicted in maps prepared by EPA and the States, respectively, are based primarily on the inclusion of “ephemeral” streams—those that only flow after rains, perhaps only once every few years—as waters of the U.S. Ephemeral streams are currently regulated in the majority of States as “waters of the State.”<sup>27</sup> Regulating these waters (which look more like land than “waters” to most people)—and any small wetlands and ponds “adjacent” to them—as WOTUS would be one of the largest regulatory expansions in history.

Although the WOTUS rule is ostensibly intended to simply clarify the scope of federal jurisdiction, the rule will federalize a much larger universe of clean water programs now run by States and localities:

- Stormwater programs run by municipalities will be required to impose more stringent controls on facilities with parking lots, storage pads, or other large paved areas. These facilities would become subject to more stringent stormwater management requirements, potentially including the requirement to obtain National Pollutant Discharge Elimination System (NPDES) permits for the first time, and to treat their stormwater before it leaves the property. This is likely to impact grocery stores, shopping centers, big box stores, stadiums, airports, schools, churches, hospitals, and many other kinds of commercial and institutional facilities;
- The revised WOTUS definition requires businesses to update and expand their Spill Prevention, Control, and Countermeasure (SPCC) Plans under section 311, and their stormwater discharge permits/plans under section 402;
- States will be immediately responsible for developing and issuing tens of thousands—maybe hundreds of thousands-- of new and revised NPDES point source permits to sources under section 402;
- States will also be required to establish water quality standards under section 303 for all newly regulated waters—including potentially 4.6 million miles of “ephemeral” tributaries, and innumerable small wetlands and ponds;

<sup>27</sup> The Association of State Wetland Managers, “Report on State Definitions, Jurisdiction, and Mitigation Requirements in State Programs for Ephemeral, Intermittent and Perennial Streams in the United States” (April 2014).

- The states will be required to certify that Federal actions meet those new water quality standards under section 401;
- The expansion of jurisdictional waters is also likely to result in a greater number of “impaired” federal waters under section 303, with additional burdens on States to evaluate and list these waters, and assign Total Maximum Daily Load (TMDL) pollutant caps to these waters; and,
- States will be required to implement their own TMDLs, or EPA-issued TMDLs, to achieve the new water quality standards for each newly regulated feature.

The states would be responsible for implementing all of these expanded duties within their existing budgets and staffing levels. Because businesses depend on being able to get state-issued permits within a reasonable timeframe, the additional workload the revised definition would place on the states would become a serious obstacle to commercial activity.

### 3. Real-World Impacts of the WOTUS Rule on Counties and Local Jurisdictions

The WOTUS rule would impose a particularly heavy regulatory burden on counties and local government jurisdictions. Much of this burden would come in the form of permits and approvals never before required to conduct routine infrastructure maintenance. According to the National Association of Counties, the nation’s counties are responsible for building and maintaining 45% of the roads in 43 states.<sup>28</sup> Because the WOTUS Rule defines “tributaries” to include ditches, flood channels, and other infrastructure, counties would immediately be required to obtain section 402 and/or 404 permits for work in those areas that may disturb soil or otherwise add any “pollutant” that could affect the “tributary.”<sup>29</sup> County irrigation districts, flood control districts, road departments, weed control districts, pest control districts, etc., would be required to obtain these permits in addition to section 402 permits for discharges to these waters.

Individual section 404 permits currently may take more than a year to obtain, and have an estimated median cost of \$155,000.<sup>30</sup> These permits are required by the CWA, regardless of the environmental benefit, if any, and permittees’ lack of resources to address this new federal requirement.<sup>31</sup>

<sup>28</sup> Testimony of Warren “Dusty” Williams, General Manager, Riverside County Flood Control & Water Conservation District, submitted on behalf of the National Association of Counties, before the House Transportation and Infrastructure Committee, Subcommittee on Water Resources and Environment (June 11, 2014) at page 2.

<sup>29</sup> The final WOTUS rule does contain some exclusions for particular features under very specific circumstances, but the exclusions are complex, require technical analyses to determine if they apply, and are likely to be interpreted very narrowly. For example, some ditches are excluded from federal jurisdiction, but only if they were not originally excavated in a “tributary” as broadly defined by the rule, not a relocated “tributary” and do not drain a wetland. 80 Fed. Reg. 31705 (June 29, 2015). However, any segment of such a ditch that intersects with a wetland is jurisdictional, and portions of the ditch up and down the stream of that wetland intersection must be assessed on a case by case basis. *Id.* at 37098.

<sup>30</sup> EPA and U.S. Army Corps of Engineers, *Economic Analysis of EPA-Army Clean Water Rule* (May 2015), available at [http://www.usace.army.mil/Portals/2/docs/civilworks/regulatory/news/final\\_CWR\\_eco\\_analysis.pdf](http://www.usace.army.mil/Portals/2/docs/civilworks/regulatory/news/final_CWR_eco_analysis.pdf).

<sup>31</sup> The Lake County, Oregon, Road Department, for example, located in a county with 7,711 residents in 2012, must maintain the county’s road network, including ditches, culverts, and bridges, with only a dozen or so employees.

### III. EPA DOES NOT FOLLOW CONGRESS' REGULATORY DIRECTIVES

Since the first agency was established, Congress has attempted to control agency rulemakings through legislation, oversight and funding, but with little to no impact. Many of the adverse impacts of regulations would have been addressed by the agencies (or at least identified) had they merely implemented congressional mandates concerning the impact on jobs, the use of the best data in rulemakings, the impact of the regulations on small business, state and local governments, and the cumulative impact of regulations. As described below, the WOTUS Rule provides a textbook example of how a federal agency failed to follow congressional directives in a significant rulemaking.

#### A. The EPA Fails to Comply with the Unfunded Mandates Reform Act

The Unfunded Mandates Reform Act ("UMRA") requires federal agencies to assess the effects of a rule on state and local governments and the private sector before imposing mandates on them of \$100 million or more per year without providing federal funding for state and local governments to implement the mandate. In essence, UMRA is intended to prevent federal agencies from shifting the costs of federal programs to the states. In the WOTUS rule, the EPA and the Corps certified that "[t]his action does not contain any unfunded mandate under the regulatory provisions of Title II of the Unfunded Mandates Reform Act of 1995, (12 U.S.C. §§ 1531-1538), and does not significantly or uniquely affect small governments."<sup>32</sup> This definitive statement is clearly at odds with the facts, however.

For example, according to the National Association of Counties, 1,542 of the 3,069 counties in the nation (50%) have populations of less than 25,000,<sup>33</sup> are considered "small governments" and are therefore protected by both the UMRA and RFA. These counties are responsible for building and maintaining 45% of the roads and associated ditches in 43 states,<sup>34</sup> which is where some of the largest permitting impacts of the WOTUS rule are expected to be felt. As a result of the WOTUS rule, these counties will be required to bear the cost of obtaining Clean Water Act permits in greatly-expanded areas, but will receive no additional federal funding for the increased responsibility imposed by the rule.

*The EPA should fulfill its statutory obligation under UMRA by not imposing unfunded mandates over \$100 million on state and local governments without providing funding.*

See [www.lakecountyor.org/government/road\\_master.php](http://www.lakecountyor.org/government/road_master.php). Brown County, North Dakota officials have also cited concerns about WOTUS permit delays "for something as simple as replacing a culvert." Gary Vetter, Assistant to the Brown County Commissioners, cited in "EPA's Proposed Definition Change Concerns County, Thune," Aberdeen News, Local News (posted August 16, 2014).

<sup>32</sup> U.S. Environmental Protection Agency & U.S. Department of the Army, Economic Analysis of the EPA-Army Clean Water Rule (May 2015), at 61, available at [http://www2.epa.gov/sites/production/files/2015-05/documents/final\\_clean\\_water\\_rule\\_economic\\_analysis\\_5-15\\_2.pdf](http://www2.epa.gov/sites/production/files/2015-05/documents/final_clean_water_rule_economic_analysis_5-15_2.pdf). See also Definition of "Waters of the United States" Under the Clean Water Act; Proposed Rule, 79 Fed. Reg. 22,220 (April 21, 2014).

<sup>33</sup> Testimony of Warren Williams, General Manager, Riverside County Flood Control & Water Conservation District, submitted on behalf of the National Association of Counties, before the House Transportation and Infrastructure Committee, Subcommittee on Water Resources and Environment (June 11, 2014) at page 2.

<sup>34</sup> *Id.*



### B. The EPA Failed to Comply with the Regulatory Flexibility Act

Congress passed the Regulatory Flexibility Act (“RFA”) in 1980 to give small entities a voice in the federal rulemaking process.<sup>35</sup> Put simply, the RFA requires federal agencies to assess the economic impact of their planned regulations on small entities and to consider alternatives that would lessen those impacts. The RFA requires each federal agency to review its proposed and final rules to determine if the rule in question will have a “significant economic impact on a substantial number of small entities.”<sup>36</sup> If the rule is expected to have such an impact, the agency must assess the anticipated economic impacts of the rule and evaluate whether alternative actions that would minimize the rule’s impact would still achieve the rule’s purpose.

Since 1996, the EPA specifically has been required to conduct Small Business Advocacy Review Panels when a planned rule is likely to have a significant impact. This process is supposed to occur before a rule is even proposed. Small entity representatives—who speak for the sectors that are likely to be affected by the planned rule—advise the Panel members on real-world impacts of the rule and potential regulatory alternatives. The Panel process is the best opportunity for the EPA to get face-to-face interaction with small entities and get a sense of the ways that small entities differ from their larger counterparts in their ability to comply with regulatory mandates. Because the Panel occurs early, before the planned rule is publicly proposed, it also represents the best opportunity for small entities to have real input into the final design of a rule.

In the case of WOTUS, the EPA certified without any factual evidence (and contrary to jurisdictional maps the agency itself generated) that the WOTUS rule actually represents a *reduction* in the regulatory burdens affecting small entities, and that the rule would not have a substantive or direct regulatory effect on any small entity, so the RFA doesn’t apply.<sup>37</sup> Yet, because the WOTUS rule defines “tributaries” to include ditches, flood channels, and other infrastructure, businesses and small governmental jurisdictions will be subject to section 404 permitting requirements for work in ditches, on roads adjacent to ditches, on culverts and bridges, etc. that disturbs soil or otherwise affects the “tributary.”<sup>38</sup> These permits can take more than a year to obtain, at a median cost of \$155,000.<sup>39</sup> This is why the U.S. Small Business Administration’s Office of Advocacy publicly advised the EPA and the Corps that they improperly certified the WOTUS proposal under the RFA.<sup>40</sup>

*The EPA should satisfy its statutory obligations under the RFA by convening a Small Business Advocacy Review Panel for important proposed regulations, like WOTUS and the Clean Power Plan.*

<sup>35</sup> 5 U.S.C. §§ 601-612.

<sup>36</sup> 5 U.S.C. §605(b).

<sup>37</sup> EPA again certified in the final WOTUS rule that the rule will not have a significant economic impact on a substantial number of small entities and that the RFA does not apply. 80 Fed. Reg. 37,102 (June 29, 2015).

<sup>38</sup> See fn 29, *supra*.

<sup>39</sup> EPA and U.S. Army Corps of Engineers, *Economic Analysis of Proposed Revised Definition of Waters of the United States* (March 2014) at 12.

<sup>40</sup> Letter from Winslow Sargeant, Chief Counsel for Advocacy, to Gina McCarthy, Administrator, EPA and General John Peabody, Deputy Commanding General, Corps of Engineers, on Definition of “Waters of the United States” Under the Clean Water Act (October 1, 2014) at 4.

### C. The EPA Fails to Follow the Information Quality Act

The Agencies' WOTUS rule neither complies with the Information Quality Act (IQA) as implemented under Office of Management and Budget (OMB) guidelines, nor EPA's own information quality guidelines.<sup>41</sup>

The Agencies developed the WOTUS Rule based upon EPA's Report, *Connectivity of Streams and Wetlands to Downstream Waters: A Review and Synthesis of the Scientific Evidence*. The Report purports to establish a scientific basis for the connectivity of isolated, often evanescent "waters" to traditional "navigable" waters under the CWA. The Agencies argue that the hydrologic "connectivity" of these remote waters, which ultimately reach navigable waters, establishes federal jurisdiction over these waters. The information contained in the Agencies' Report clearly meets the OMB definition of "information." "Information" means any communication or representation of knowledge such as facts or data, in any medium or form, including textual, numerical, graphic . . . .<sup>42</sup>

The information at issue also meets the OMB definition of "influential" information. "Influential" means "that the agency can reasonably determine that the dissemination of the information will have or does have a clear and substantial impact on important public policies . . . ."<sup>43</sup> The Agencies have directly relied upon the Report in making findings regarding the extent of hydrologic connectivity sufficient to support an assertion of federal jurisdiction. OMB has stated that "influential information" should be held to a heightened standard of quality.<sup>44</sup> The Report clearly meets the definition of "influential" information that needs to be of the highest quality.

On the date the Agencies published the proposed WOTUS rule, EPA's Science Advisory Board (SAB) had not completed its review of the Report. In fact, the SAB did not complete its review of the Report until September 30, 2014. EPA and the Corps ultimately extended the public comment period until November 14, 2014. But commenters had no opportunity to consider EPA's response to the SAB, and only a limited time to review the final Report before the opportunity to comment had ended. EPA and the Corps should have re-proposed the rule with an updated discussion of the Report, or alternatively, the agencies should have extended the public comment period further to allow for informed input from stakeholders on the information quality of the Report.

*The EPA should follow the IQA by fully disclosing data and reports used to justify its positions and utilizing the best peer-reviewed science.*

<sup>41</sup> See Treasury & General Governmental Appropriations Act for Fiscal Year 2001, Pub. L. No. 106-554 § 515(a); 44 U.S.C. § 3516 (notes); EPA Guidelines for Ensuring and Maximizing the Quality, Objectivity, Utility and Integrity of Information Disseminated by the Environmental Protection Agency, EPA/260R-02-2008 (October 2002).

<sup>42</sup> OMB Guidelines § V.5.

<sup>43</sup> OMB Guidelines § V.9

<sup>44</sup> 67 Fed. Reg. 8,452 (February 22, 2002).

#### **D. EPA Has Failed to Conduct the Congressionally Mandated Employment Impacts Evaluation**

Congress has debated whether environmental regulations cause job loss and adversely impact communities since the first environmental laws were debated in the early 1970's. During the debate over the 1972 Clean Water Act claims were raised by industry that environmental regulations cost jobs. While there was great debate over the issue, Congress specifically wanted to resolve this issue of whether environmental regulations cost jobs.

Congress addressed this issue five times over two decades by placing similar provisions in the five major environmental statutes directing EPA to conduct continuing evaluations on potential loss or shifts in employment which may result from the issuance of regulations under the respective statutes. The congressional intent behind these provisions is clear: Congress knew that regulations, such as those issued under the Clean Water Act and Clean Air Act, would impact the operations of facilities, cause loss of job, and adversely impact communities but it did not know if such losses were the primary cause or if there were other causes. Congress wanted to resolve this issue but it needed information from the agencies issuing the regulations.

During the 92<sup>nd</sup> Congress (1971 – 1973), the debate over the Federal Water Pollution Control Act Amendments of 1972 addressed this issue for the first time. As part of the floor debate, Representative William D. Ford of Michigan offered an amendment mandating the continuous evaluation of the potential loss or shifts of employment resulting from the issuance of water regulations.<sup>45</sup> In support of the amendment, Representative Bella Abzug of New York stated:

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<sup>45</sup> 33 U.S.C. § 1367(e) (1972)(e) Investigations of Employment Reductions, The Administrator shall conduct continuing evaluations of potential loss or shifts of employment which may result from the issuance of any effluent limitation or order under this chapter, including, where appropriate, investigating threatened plant closures or reductions in employment allegedly resulting from such limitation or order. Any employee who is discharged or laid-off, threatened with discharge or lay-off, or otherwise discriminated against by any person because of the alleged results of any effluent limitation or order issued under this chapter, or any representative of such employee, may request the Administrator to conduct a full investigation of the matter. The Administrator shall thereupon investigate the matter and, at the request of any party, shall hold public hearings on not less than five days notice, and shall at such hearings require the parties, including the employer involved, to present information relating to the actual or potential effect of such limitation or order on employment and on any alleged discharge, lay-off, or other discrimination and the detailed reasons or justification therefor. Any such hearing shall be of record and shall be subject to section 554 of title 5. Upon receiving the report of such investigation, the Administrator shall make findings of fact as to the effect of such effluent limitation or order on employment and on the alleged discharge, lay-off, or discrimination and shall make such recommendations as he deems appropriate. Such report, findings, and recommendations shall be available to the public. Nothing in this subsection shall be construed to require or authorize the Administrator to modify or withdraw any effluent limitation or order issued under this chapter.) In subsequent statutes the job impact provision was split into two sections; one mandating the continuous evaluation of job impacts and one section authorizing employees impacted by the regulation to seek an on the record hearing with the administrator of EPA. See also: <sup>45</sup> The Clean Air Act, 42 U.S.C. § 7621(a), (1977); § 321(a); The Solid Waste Disposal Act, 42 U.S.C. § 6971 (1976); § 7001(e); The Toxic Substances Control Act, 15 U.S.C. § 2623 (1976); § 24(a); the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. § 9610 (1980); § 110(e).

Mr. Chairman, I am pleased to rise in support of the amendment, which would require the Environmental Protection Administration to study and evaluate, on a continuing basis, the effect of effluent limitations upon employment...this amendment will allow Congress to get a close look at the effects on employment of legislation such as this, and will thus place us in a position to consider such remedial legislation as may be necessary to ameliorate those effects. This is a good amendment and I urge its adoption.<sup>46</sup>

This amendment laid the framework for similar provisions in future legislation.<sup>47</sup>

The 95<sup>th</sup> Congress (1977 – 1979), again addressed the effects of regulation on employment in debate over the Clean Air Act. The Committee on Public Works noted:

[I]t has been argued that environmental laws have in fact been responsible for significant numbers of plant closings and job losses. In any particular case in which a substantial job loss is threatened, in which a plant closing is blamed on Clean Air Act requirements, or possible new construction is alleged to have been postponed or prevented by such requirements, the committee recognized the need to determine the truth of these allegations. For this reason the committee agreed to...a mechanism for determining the accuracy of any such allegation.<sup>48</sup>

In the Clean Air Act Amendments of 1977 Congress enacted a similar provision mandating EPA to conduct continuous evaluations of potential loss or shifts of employment.<sup>49</sup> That provision is codified as section 321(a) of the Clean Air Act, which reads:

**(a) Continuous Evaluation of Potential Loss or Shifts of Employment**

The Administrator shall conduct continuing evaluations of potential loss or shifts of employment which may result from the administration or enforcement of the provision of this chapter and applicable implementation plans, including where appropriate, investigating threatened plant closures or reductions in employment allegedly resulting from such administration or enforcement.<sup>50</sup>

Subsequent Congresses enacted similar legislative provisions in the Solid Waste Disposal Act,<sup>51</sup> the Toxic Substances Control Act,<sup>52</sup> and the Comprehensive Environmental Response, Compensation and Liability Act.<sup>53</sup>

<sup>46</sup> 1 Environmental Policy Division of the Cong. Research Serv., A Legislative History of the Water Pollution Control Act Amendments of 1972, at 658-59 (1973) (Remarks of Rep. Abszug).

<sup>47</sup> See 95 Cong. House Report 294 (Stating that "Section 304 of the committee bill [the Clean Air Act] is based on a nearly identical provision in the Federal Water Pollution Control Act.")

<sup>48</sup> *Id.*

<sup>49</sup> See generally 95 Cong. Conf. Bill H.R. 6161; CAA 77 Leg. Hist. 24.

<sup>50</sup> 42 U.S.C. § 7621(a) (1977); § 321(a).

<sup>51</sup> 42 U.S.C. § 6971 (1976); § 7001(e).

<sup>52</sup> 15 U.S.C. § 2623 (1976); § 24(a).

<sup>53</sup> 42 U.S.C. § 9610 (1980); § 110(e).

Unfortunately, EPA never conducted any of the evaluations of employment impacts required by the five environmental statutes. In response to a Freedom of Information Act request from the U.S. Chamber, EPA states that it cannot find any records that indicate it prepared a continuing evaluation of the potential loss or shifts of employment resulting from its regulations. Specifically, EPA stated: “after conducting searches, neither the Office of Air and Radiation nor the Office of Policy were able to find any documents pertaining to your request”.<sup>54</sup>

Therefore, the debate that started over 45 years ago and which resulted in Congress enacting provisions that would help it understand the adverse effects that environmental regulation have on employment remains unresolved due to EPA’s failure to undertake the evaluations mandated multiple times by Congress. Congress wanted information to develop remedial legislation, if needed to protect jobs while it protects the environment.

*The EPA must comply with its statutory obligation under the Clean Water Act and conduct a continuing evaluation of the employment impacts of CWA regulations.*

#### **E. The EPA Failed to Examine Inconsistent or Incompatible Regulations as Required by Executive Order 12,866**

Executive Order 12,866<sup>55</sup> requires federal agencies to conduct several analyses prior to proposing or finalizing new regulations. The Executive Order makes agencies responsible to ensure that a new regulation is necessary (as opposed to a non-regulatory alternative); put another way, the agency must show that a problem exists that can **only** be successfully addressed through a regulation. In the case of the WOTUS rule, neither EPA nor the Corps showed that waters currently regulated by states and localities are not adequately protected. EPA and the Corps did not explain how the public would be better off if waters regulated by the states were transformed into areas under federal jurisdiction. Although EPA and the Corps *inferred* that the states were not doing an adequate job of protecting surface waters, it did not make the kind of showing that would typically be required to take federal control over a state’s water quality program.<sup>56</sup> Similarly, the ozone NAAQS was updated in 2015 before the 2008 standard was even fully implemented.

In the case of WOTUS, the final rule was issued at a time when two other major rules (Clean Power Plan and the Ozone NAAQS standard) were also issued. To be clear, during a six-month period of time in 2015, EPA imposed on the states three major rules that have significant impacts on this nation’s economy and infrastructure. When issuing these three rules in 2015, the EPA should have fully considered how each rule, if finalized, might affect regulated entities’ ability to comply with the other two.

<sup>54</sup> Letter from Jim DeMocker, Acting Director, EPA Office of Policy Analysis and Review to William L. Kovacs, U.S. Chamber of Commerce, Freedom of Information Request No. EPA-HQ-2012-001352 (June 14, 2013).

<sup>55</sup> See Executive Order 12,866 (Sept. 30, 1993) available at [https://www.whitehouse.gov/sites/default/files/omb/inforeg/EO12866/EO12866\\_10041993.pdf](https://www.whitehouse.gov/sites/default/files/omb/inforeg/EO12866/EO12866_10041993.pdf).

<sup>56</sup> 33 U.S.C. § 304(l)(3).

For example, the EPA itself projects that the Clean Power Plan will cause significant coal-fired electric generating capacity to retire by 2022.<sup>57</sup> To replace this generating capacity, utilities will need to construct fuel delivery infrastructure such as pipelines, storage, railroad track, and improved roads. In order to compensate for a lack of generating capacity, these infrastructure projects will have to be completed before the existing coal-fired generating units are taken off-line. Yet these projects will be subject to more extensive permitting and reviews by virtue of the WOTUS rule.

The EPA did not properly account for the increased costs and delays that utilities, pipeline companies, railroads, and other companies will face in complying with the WOTUS rule, which is made necessary because of the need to comply with the Clean Power Plan.

*The EPA must consider whether a conflict exists regarding regulated entities' ability to comply with stricter ozone standards, the redefinition of WOTUS, and the Clean Power Plan at the same time pursuant to Executive Order 12,866.*

#### **F. The EPA Failed to Analyze the Cumulative Impacts of the Regulations as Required by Executive Order 13,563**

Executive Order 13,563, issued by the Obama administration in 2011,<sup>58</sup> even more clearly calls on federal agencies to review and understand the cumulative impacts of their regulatory programs. Section 1(b)(2) provides that each agency must, among other things, “tailor its regulations to impose the least burden on society, consistent with obtaining regulatory objectives, *taking into account, among other things, and to the extent practicable, the costs of cumulative regulations.*”<sup>59</sup> Again, the EPA should have complied with this Executive Order when it planned to develop three massive rulemakings that would be timed to take effect virtually one on top of the other.

*The EPA pursuant to Executive Order 13,563 should conduct a cumulative review of costs imposed on regulated entities by the almost simultaneous impact of stricter ozone standards, the redefinition of WOTUS, and the Clean Power Plan.*

#### **G. What the EPA Would Have Discovered If It Had Used Congressionally and Executive Mandated Analytical Regulatory Tools**

If the EPA had chosen not to ignore the vast array of analytical requirements under the Clean Water Act, the Unfunded Mandates Reform Act; the Information Quality Act, and the Regulatory Flexibility Act, as well as Executive Orders 12,866 and 13,563, it would have discovered serious inconsistencies and conflicts between its three rules. Here are two examples of those inconsistencies as they relate to WOTUS specifically:

<sup>57</sup> See EPA, “Regulatory Impact Analysis for the Clean Power Plan Final Rule,” (October 23, 2015) available at <https://www.epa.gov/sites/production/files/2015-08/documents/cpp-final-rule-ria.pdf>.

<sup>58</sup> Executive Order 13,563, “Improving Regulatory and Regulatory Review,” 76 Fed. Reg. 3,821 (Jan. 18, 2011).

<sup>59</sup> *Id.* at 3,821 (emphasis added).

- As noted above, the massive new infrastructure requirements that are at the heart of the Clean Power Plan will be complicated, delayed and made more expensive by the expanded number of Clean Water Act permits required by the WOTUS rule. In addition to the cost of applying for federal permits, infrastructure developers will have to pay mitigation costs for wetlands restoration, which often approach or exceed all other project costs.
- In its economic analysis of the WOTUS rule, the EPA based its conclusion that the rule would only increase the amount of federal jurisdictional waters under the CWA by 2.84% to 3.65% on a *very* small sample of negative determinations from two preceding years, essentially using just a tiny slice of pre-WOTUS determinations. The EPA ignored conflicting evidence from federal and state authorities that the rule could impose anywhere from a 300% to 800% increase in federal jurisdictional waters. EPA is supposed to work with these stakeholders to discuss these impacts, instead of ignoring them or denying them altogether. By ignoring these congressional mandates for developing effective regulations, the EPA fails to secure an understanding of the real world impacts of its rules.

Undoubtedly, more examples of inconsistencies will be discovered as these three major regulations continue to move through the regulatory and judicial process and eventually must be implemented. Much of the confusion and deficiencies stemming from these inconsistencies could have been avoided had the EPA conducted a more thorough analysis of the cumulative impacts of these regulations.

#### H. EPA Violated Anti-Lobbying Laws

In addition to the legal and procedural deficiencies described above, the U.S. Government Accountability Office (GAO) also determined that during the rulemaking process, EPA violated prohibitions against publicity or propaganda and grassroots lobbying and violated the Antideficiency Act, 31 U.S.C. sec. 1341(a)(1)(A).<sup>60</sup> In particular, the GAO determined that EPA's use of a Thunderclap social media campaign during the rulemaking process was unlawful. Thunderclap is a social media tool that first gathers "supporters" for a particular cause, then simultaneously blasts a message to each supporter's social media accounts, including Facebook, Twitter, and Tumblr.<sup>61</sup> The purpose is to have the original message reach everyone who views its supporters' social media pages. Accordingly, EPA first solicited and secured 980 supporters for its message promoting the WOTUS rule. However, and crucial to this analysis, when EPA's message was re-posted on supporters' accounts using Thunderclap, the message no longer identified EPA as the source. The GAO determined that these unattributed messages constituted "covert propaganda" and violated the Antideficiency Act.<sup>62</sup> According to the GAO, the improper communications associated with the Thunderclap campaign were estimated to have reached 1.8 million people.<sup>63</sup>

<sup>60</sup> B-326944, Dec. 14, 2015 (Environmental Protection Agency – Application of Publicity or Propaganda and Anti-lobbying Provisions).

<sup>61</sup> [www.thunderclap.it/faq](http://www.thunderclap.it/faq)

<sup>62</sup> B-326944, Dec. 14, 2015.

<sup>63</sup> *Id.* at 12.

Illegally soliciting support for the WOTUS rule from 1.8 million people is significant. A total of 1,081,166 public comments were received on the WOTUS rulemaking docket. Of those, approximately 1,050,000 comments were generated from mass comment campaigns. In the final WOTUS rule preamble, EPA relied upon that large number of public comments received to support finalizing the rule. Indeed, the Federal Register states that that “over 1 million public comments” were received on the proposed WOTUS rule, and “the substantial majority of which supported the proposed rule.” 80 Fed. Reg. 37,057. These statements are now part of the official rulemaking record, which the agency is using to defend its rule in the ongoing WOTUS litigation.

EPA Administrator McCarthy also testified before Congress about the purported wide public support for the rule, “we have received over one million comments and about 87.1 percent of those comments we have counted so far – we are only missing 4,000 – are supportive of this rule. Let me repeat, 87.1 percent of those one plus million are supportive of this rule.”<sup>64</sup>

In sum, EPA unlawfully solicited support from 1.8 million people for its WOTUS rule. EPA then relied on more than one million mass mailing comments in support to justify its WOTUS rule to the public, before Congress, and will no doubt use the same ginned up “support” to defend the WOTUS rule in court.

In addition to using Thunderclap, EPA hyperlinked official EPA websites and social media pages to external websites that contained clear appeals to the public to contact Members of Congress in support of the WOTUS rule.<sup>65</sup> The GAO found this activity constituted indirect or grassroots lobbying, in violation of the anti-lobbying provisions of the law.

#### IV. THE WOTUS RULE CAUSES MASSIVE CONFUSION

Shortly after the WOTUS rule was finalized, lawsuits were filed by at least thirty states and numerous industry groups and environmentalists, all objecting to the scope of the rule or the process by which it was promulgated. Lawsuits were filed in at least twelve different federal district courts and in eight different federal circuit courts of appeal.

Lawsuits were filed in both district courts and courts of appeal because there is no agreement as to which court even has jurisdiction to hear the case. For example, the district court in North Dakota issued an injunction that prevents the rule from being implemented or enforced within the thirteen states that filed lawsuits in North Dakota. The Southern District of Georgia, however, denied a motion for injunction on the grounds that jurisdiction is proper at the court of appeal level; this decision has been appealed to the Eleventh Circuit.

<sup>64</sup> *House-Senate Joint Hearing on State and Local Impacts of Administration's Proposed Expansion of Waters Regulation Before the S. Comm. on Environment and Public Works and H. Comm. on Transportation and Infrastructure*, 114<sup>th</sup> Cong. (Feb. 4, 2015) (Statement of Gina McCarthy, Administrator of the Environmental Protection Agency).

<sup>65</sup> B-326944, Dec. 14, 2015.



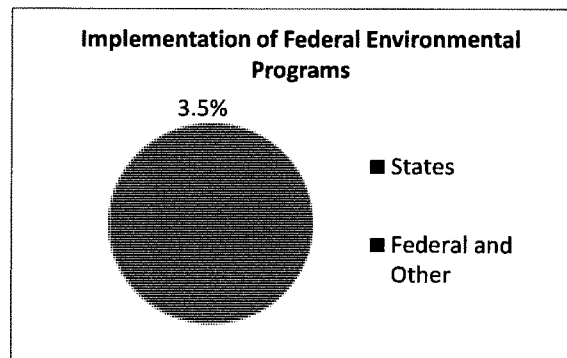
Meanwhile, the lawsuits filed in the courts of appeal have been consolidated and will all be heard in the Sixth Circuit. The Sixth Circuit issued a nationwide injunction of the rule, preventing EPA and the Army Corps from implementing or enforcing the WOTUS rule during the pendency of litigation. A three-judge panel of the Sixth Circuit recently issued a fractured ruling (with three separate opinions) concluding that court has jurisdiction. But parties (including the U.S. Chamber) have requested a rehearing of the jurisdictional issue before the entire Sixth Circuit.

Landowners are now waiting for a decision on the merits of whether the WOTUS rule is lawful or if the agencies must once again start from scratch. The confusion created by the WOTUS rule and the varied potential outcomes of the resulting litigation translate into an environment of uncertainty for landowners and business owners.

#### V. STATES IMPLEMENT MOST FEDERAL ENVIRONMENTAL REGULATIONS, NOT THE EPA

The real victims of the federal administrative state overreach are the states. According to the Environmental Council of the States (ECOS), the states in 2013 implemented approximately 96.5% of federal environmental laws through delegated programs.<sup>66</sup> State agencies also conduct 90% of all environmental inspections, enforcement actions, data collection, and issue the vast bulk of the permits needed to build or operate a facility.<sup>67</sup>

Figure 5:



Source: ECOS

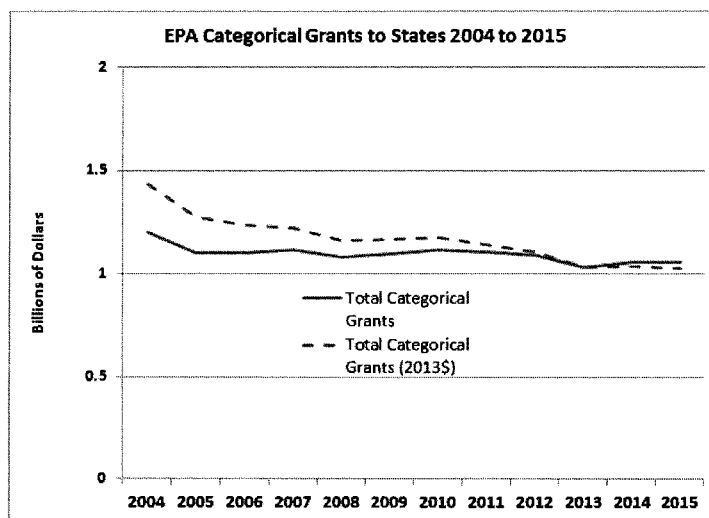
<sup>66</sup> Testimony of Teresa Marks, Director, Arkansas Department of Environmental Quality and President, Environmental Council of the States, before the House Energy and Commerce Committee, Subcommittee on Environment and the Economy (February 15, 2013) at 3, available at <http://docs.house.gov/meetings/IF/IF18/20130215/100242/HHRG-113-IF18-Wstate-MarksT-20130215.pdf>.

<sup>67</sup> *Id.*

In a February 15, 2013 hearing before the House Committee on Energy and Commerce, Subcommittee on Environment and the Economy, an ECOS witness testified that “[S]tates find themselves in 2013 with a lot more [environmental] rules, and the possibility of a lot less money to implement them. States are very unsure how much longer these two trends can continue before the core environmental programs in each state begin to significantly suffer.”<sup>68</sup>

The management of federal environmental programs is a tremendous burden for states, particularly from a time, money and resource perspective. To add to the difficulties that states face, annual budget data collected by the Congressional Research Service between 2004 and 2015 confirms that EPA grants to the states have been flat or, in real terms have steadily declined since 2004.<sup>69</sup> In 2015, Categorical Grants to the states, the federal funding to states for implementation of EPA regulatory mandates, were about 29% lower in inflation-adjusted dollars than they were in 2004.

Figure 6:



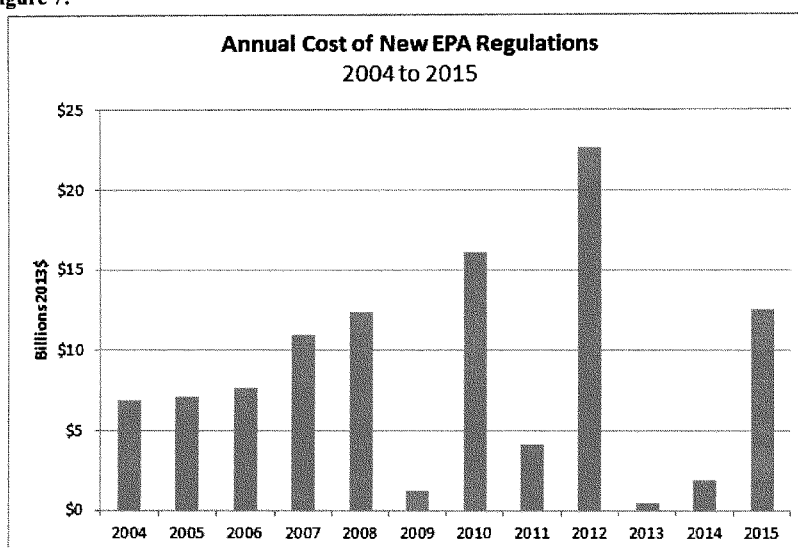
Source: Congressional Research Service

<sup>68</sup> Testimony of Teresa Marks, Director, Arkansas Department of Environmental Quality and President, Environmental Council of the States, before the House Energy and Commerce Committee, Subcommittee on Environment and the Economy (February 15, 2013) (emphasis added), available at <http://docs.house.gov/meetings/IF/IF18/20130215/100242/HHRG-113-IF18-Wstate-MarksT-20130215.pdf>.

<sup>69</sup> Likewise, a 2013 GAO report noted that “annual appropriations for these grants have decreased by approximately \$85 million between fiscal year 2004 and fiscal year 2012.” GAO, *Funding for 10 States’ Programs Supported by Four Environmental Protection Agency Categorical Grants*, 13-504R Information on EPA Categorical Grants (May 6, 2013).

At the same time that EPA's real-dollar grant assistance to the states declined **29%**, the agency imposed approximately **\$104 billion** in new annual regulatory obligations (see Figure 7).

**Figure 7:**



Source: EPA Regulatory Impact Analyses (RIAs) and *Federal Register*

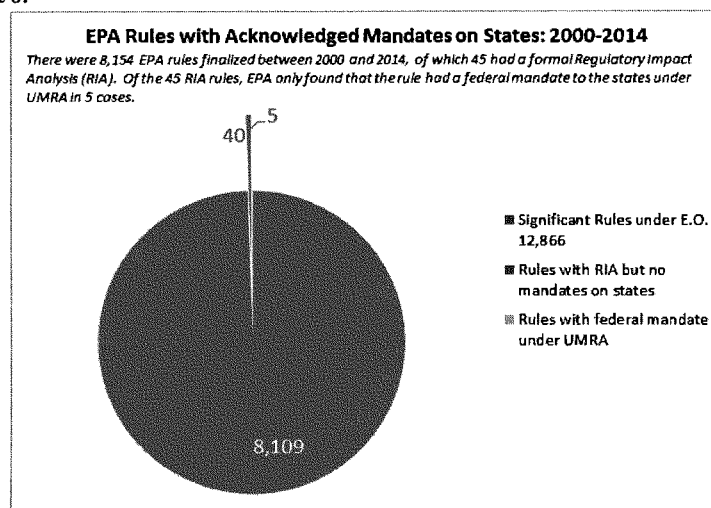
Significantly, as described above, in 2015 alone, EPA issued three new “mega-rules” that impose tremendous burdens on the states: WOTUS,<sup>70</sup> the Clean Power Plan,<sup>71</sup> and the revised Ozone NAAQS.<sup>72</sup> Although each of these rulemakings imposes major new responsibilities on states, the agency certified in each case that the regulation imposed **no unfunded mandates**. In fact, the EPA has seldom acknowledged that any of its regulations impose unfunded mandates on the states.

<sup>70</sup> EPA and U.S. Army Corps of Engineers, “Definition of “Waters of the United States,” Final Rule, 80 Fed. Reg. 37,054 (June 29, 2015).

<sup>71</sup> EPA, “Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units,” Final Rule, 80 Fed. Reg. 64,662 (October 23, 2015).

<sup>72</sup> EPA, “National Ambient Air Quality Standard for Ozone,” Final Rule, 80 Fed. Reg. 65,292 (October 26, 2015).

Figure 8:



Source: EPA Regulatory Impact Analyses (RIAs) and Federal Register

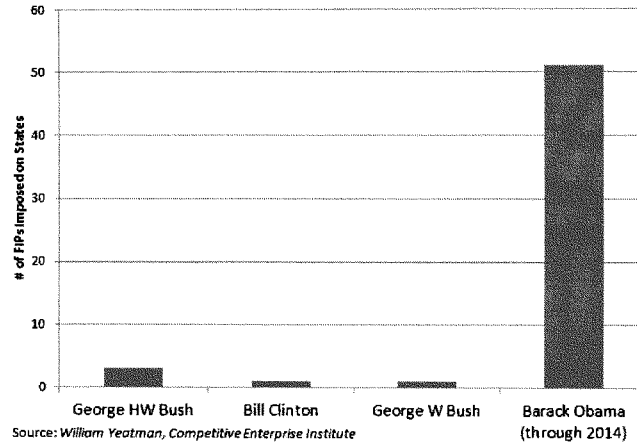
States have complained in recent years that EPA increasingly ignores them or takes unilateral actions that the states disagree with. Rather than being treated by EPA as co-regulators with complementary powers, states complain that their views and concerns are increasingly ignored by EPA. As one state official put it, “the State role is now **less partner and more pawn**.”<sup>73</sup> EPA’s failure to consult with the states violates the spirit, if not the letter, of Executive Order 13,132, “Federalism.”<sup>74</sup>

One result of EPA’s failure to adequately consult with its state partners is a substantial increase in the number of Federal Implementation Plans (FIPs), representing an unprecedented federal takeover of state environmental priorities and programs. As the chart below clearly shows, the EPA under the current Administration has in fact imposed far more FIPs on states than any previous administration, ever. These FIPs include 13 dealing with regional haze, 9 relating to greenhouse gas permitting programs, and 28 for the cross-state air pollution rule.

<sup>73</sup> Letter from Becky Keogh, Director, Arkansas DEQ to Senator James M. Inhofe, Chairman, Senate Committee on Environment and Public Works (March 2, 2016) at 1 (emphasis added). Available at <http://www.epw.senate.gov/public/cache/files/89138698-8bc6-4cec-b624-eebe81b3e251/arkansas.pdf>.

<sup>74</sup> 64 Fed. Reg. 43,255 (August 10, 1999).

Figure 9:

**Clean Air Act FIPs by Administration**

By requiring states to implement WOTUS, Clean Power Plan, and ozone NAAQS simultaneously, the inconsistent segments of each statute make planning impossible. While the EPA ignored potential inconsistencies created by issuing all three rules simultaneously, states simply cannot ignore the problems of implementing all three at the same time. For example, in writing a State Implementation Plan (SIP) for the Ozone NAAQS, states cannot ignore the probable shifts in criteria pollutant levels resulting from the Clean Power Plan and the expanded redefinition of WOTUS. Because the Clean Power Plan could require significant changes to the nation's electric generation infrastructure, reshuffling of the deck would dramatically shift the current map of criteria pollutant concentrations as power companies site new generation facilities away from existing sites. In particular, this could undermine the ability of many states to meet the current air and water standards as the states simultaneously implement WOTUS, Clean Power Plan, and ozone NAAQS.

## VI. LEGISLATIVE RECOMMENDATION

### **The Regulatory Accountability Act Requires More Extensive Rulemaking Procedures for the Most Important New Federal Rules**

A modernized APA is needed to restore the kinds of checks and balances on federal agency action that the 1946 APA—the “bill of rights” for the regulatory state—intended to provide the American people. Congress must get the rulemaking process right since poorly written rules flood the federal judicial system as judges are asked to do the job that agencies

should. S. 2006, the Regulatory Accountability Act of 2015, which rests in the jurisdiction of this committee, would address this deficiency. The legislation would put balance and accountability back into the federal rulemaking process for the most critical rules, without undercutting vital public safety and health protections. The bill focuses on the process agencies (including independent agencies) must use when they write the most important new regulations. The Regulatory Accountability Act would achieve these important goals for major and high-impact rules by requiring the following:

- Defining “high-impact” rules as a way to distinguish the 1-3 rulemakings each year that would impose more than \$1 billion a year in compliance costs.
- Codifying many of the regulatory requirements in Executive Order 12866 and applying them to both executive and independent agencies.
- Involving the public early in the process by allowing the public to propose alternatives for accomplishing the objectives in the most effective manner.
- Requiring agencies to select the least costly regulatory alternative that achieves the regulatory objective, unless the agency can demonstrate that a more costly alternative is necessary to protect public health, safety, or welfare.
- Requiring agencies to consider the cumulative impacts of regulations and the collateral impacts their rules will have on businesses and job creation.
- Providing for on-the-record administrative hearings for the 1-3 most costly rules each year to verify that the proposed rule is fully thought out and well-supported by good scientific and economic data.
- The rulemaking should be based upon the best available scientific, technical or economic information.
- Restricting agencies’ use of “interim final” regulations, where the public has no opportunity to comment before a regulation takes effect.
- Independent agencies would also have to comply with the new APA requirements.

*For the most costly rules, the opportunity for a hearing – with the ability to ask specific questions to the agency – gives stakeholders the best way to verify the underlying data an agency relies on, as well as the regulatory alternative the agency selected.* In typical APA notice and comment rulemaking also known as “informal rulemaking,” the agency is free to discount written comments and information with which it does not agree. Stakeholders have a very limited ability to inquire directly of the agency why various choices were made and get a response. Even if those stakeholders get contrary data or other information into the rulemaking docket, a reviewing court typically defers to the agency’s determination of which data to rely on. Under S. 2006, however, interested parties in the most costly rulemakings can petition the

agency to probe the data and evidence an agency is using through an administrative hearing.<sup>75</sup> This hearing would be on-the-record, meaning that a transcript of the proceedings would become part of the docket for the rulemaking. This transcript would be available for any subsequent legal challenges to the rule.

In rulemakings involving the most costly regulations (*\$1 billion or more* per year), where there is concern about whether an agency has grounded its regulation on adequate, reliable data and whether the agency has fully considered reasonable alternatives, an on-the-record hearing is the most effective way to ensure that these critical issues are explored in a manner that is open and transparent.

The Occupational Safety and Health Act (OSHA) currently provides for a similar type of hybrid hearing at the request of interested parties.<sup>76</sup> Experience with these hearings has shown that they have minimal impact on an agency's ability to issue rules in a timely fashion. Indeed, in what was perhaps the highest profile example—the ergonomics regulation proposed at the end of the Clinton administration—the agency published the proposal, held a hearing, and issued the final rule **within one year**, even though it was one of the most complicated and controversial regulations in the agency's history.<sup>77</sup>

Hearings on the record are commonplace for other types of administrative proceedings, even relatively routine ones. The U.S. Department of Agriculture, Agricultural Marketing Service, for example, uses on the record hearings as part of the process of issuing milk pricing regulations. This type of hearing is particularly useful because it defines the facts that either support or call into question the proposed regulation. This type of hearing also focuses the relevant facts through truth testing, and it confines the facts upon which a rule may be issued to those within the hearing record. This process produces a hearing record that will be invaluable to a reviewing court.

## VII. CONCLUSION

The goal of a regulatory agency should be to produce regulations that implement the intent of Congress in the most effective and efficient ways possible. Congress has provided significant guidance as to the analyses agencies must undertake to achieve Congressional intent. The analyses required by Congress are supposed to guide the agency to make decisions based on fact, sound science and economic reality.

Unfortunately, over the decades, the EPA has ignored the guidance given by Congress and Executive Order for developing rules in a cost-effective manner that achieve congressional intent. The result of such conduct is an agency that issues massive mandates that the states and

<sup>75</sup> In the case of major rules, a stakeholder could petition for the hearing, which the agency can deny.

<sup>76</sup> 29 U.S.C. § 655(b)(3). See also 29 C.F.R. §§ 1911.15-18. Other statutes require agencies to provide formal or "hybrid" rulemakings: 15 U.S.C. § 57a(c)(2)(B)(Federal Trade Commission); 21 U.S.C. § 371(e)(Food and Drug Administration); and 15 U.S.C. § 2603(b)(5)(EPA Toxic Substances Control Act).

<sup>77</sup> The controversial ergonomics rule is the only rule to be formally disapproved by Congress and the Executive under the Congressional Review Act. See S. J. Res. 5, which became Public Law 107-5 (Signed by President Bush on March 20, 2001).

the business community must implement regardless of cost. As such, EPA becomes the primary lawmaker on environmental issues, not Congress. This is a travesty and Congress must regain its role as the primary legislative body.

There is an even deeper harm however, inflicted by the EPA's failure to fully analyze the impact of its regulations. That harm is the deliberate avoidance of any attempt to understand real world impacts of regulations on people and the communities that will be adversely impacted by its actions. If the goal of every agency is to produce quality rules that implement the intent of Congress, why would an agency fail to evaluate job impacts, the cumulative impacts of regulations, develop regulations using peer reviewed studies, and use the best science and economics? The Regulatory Accountability Act of 2015 would bring the Administrative Procedure Act of 1946 into the modern era. The Regulatory Accountability Act passed the House of Representatives on January 13, 2015 by a bipartisan vote of 250-175.<sup>78</sup> The Senate has the opportunity to make this reform a reality and should take up and pass S. 2006 as soon as possible.

Thank you for allowing me to testify today and I look forward to answering your questions.

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<sup>78</sup> The House passed previous versions of Regulatory Accountability Act in 2011 and 2013. H.R. 3010, the Regulatory Accountability Act of 2011, passed the House on a bipartisan 253-157 vote on December 2, 2011. H.R. 2122, the Regulatory Accountability Act of 2013, passed the House as part of H.R. 2804, the ALERRT Act, on a bipartisan vote of 236-179 on February 27, 2014. The Senate versions of those bills, S. 1606 and S.1029, were not acted upon.



Written Testimony of  
**Robert Weissman**  
**President, Public Citizen**  
before the  
**The Senate Committee On Homeland Security and Government Affairs**  
on  
“The Administrative State: An Examination of Federal Rulemaking”  
April 20, 2016



Mr. Chairman and Members of the Committee,

Thank you for the opportunity to testify today on regulatory policy issues. I am Robert Weissman, president of Public Citizen. Public Citizen is a national public interest organization with more than 400,000 members and supporters. For 45 years, we have advocated with some considerable success for stronger health, safety, consumer protection and other rules, as well as for a robust regulatory system that curtails corporate wrongdoing and advances the public interest.

Public Citizen chairs the Coalition for Sensible Safeguards (CSS). CSS is an alliance of more than 75 consumer, small business, labor, scientific, research, good government, faith, community, health and environmental organizations joined in the belief that our country's system of regulatory safeguards provides a stable framework that secures our quality of life and paves the way for a sound economy that benefits us all. Time constraints prevented the Coalition from reviewing my testimony in advance, and today I speak only on behalf of Public Citizen.

Over the last century, and up to the present, regulations have made our country stronger, better, safer, cleaner, healthier and more fair and just. Regulations have made our food supply safer; saved hundreds of thousands of lives by reducing smoking rates; improved air quality, saving hundreds of thousands of lives; protected children's brain development by phasing out leaded gasoline; saved consumers billions by facilitating price-lowering generic competition for pharmaceuticals; reduced toxic emissions into the air and water; empowered disabled persons by giving them improved access to public facilities and workplace opportunities; guaranteed a minimum wage, ended child labor and established limits on the length of the work week; saved the lives of thousands of workers every year; protected the elderly and vulnerable consumers from a wide array of unfair and deceptive advertising techniques; ensured financial system stability (at least when appropriate rules were in place and enforced); made toys safer; saved tens of thousands of lives by making our cars safer; and much, much more.

The benefits of rules adopted during the Obama administration, as with rules adopted during the Bush administration, vastly exceed the costs, even when measured according to corporate-friendly criteria.

We have also seen in recent years with great clarity the impact of regulatory failure—lack of regulatory enforcement, regulations delayed or rolled back, and insufficient regulatory standards and protections in place. Most notably, it was regulatory failure that was significantly responsible for the Great Recession, which imposed far greater costs on the economy and cost far more jobs than regulations ever could.

To review the facts of how regulation strengthens our country and safeguards jobs, however, is not to suggest that all is well with the regulatory system. There is a need for significant regulatory reform—including reforms to reduce regulatory delay, toughen regulatory enforcement, the imposition of inappropriate analytic obligations on agencies, address imbalances in judicial review of agency rulemaking, and address anti-competitive practices that injure small businesses, consumers and the national economy.

The first section of this testimony argues that regulatory benefits vastly exceed costs and that regulatory failure—inadequate rules, and too little regulatory enforcement—should be understood as a key cause of the Great Recession and ongoing economic weakness. The second reviews the rulemaking experience with the three rules on which this hearing is focused: The fiduciary rule, the Net Neutrality rule, and the Clean Water Rule. The third section of the testimony focuses on needed reforms to strengthen our regulatory system – especially combating needless delay -- so that it fulfills its role of protecting the American people and strengthening our economy.

## I. Regulations are Economically Smart

### A. Regulatory benefits vastly exceed costs

Rhetorical debates and cost-benefit abstractions can obscure the dramatic gains our country has made due to regulation. Regulation has:

- Made our food safer.<sup>1</sup>
- Saved tens of thousands of lives by making our cars safer.<sup>2</sup>
- Made it safer to breathe, saving hundreds of thousands of lives annually.<sup>3</sup>
- Protected children's brain development by phasing out leaded gasoline and dramatically reducing average blood levels.<sup>4</sup>
- Empowered disabled persons by giving them improved access to public facilities and workplace opportunities, through implementation of the Americans with Disabilities Act.<sup>5</sup>
- Guaranteed a minimum wage, ended child labor and established limits on the length of the work week.<sup>6</sup>

<sup>1</sup> American Public Health Association. (2010, November 30). *APHA Commends Senate for Passing Strong Food Safety Legislation*. Retrieved 24 February, 2012, from [http://www.makeourfoodsafes.org/tools/assets/files/APHA\\_Senate-Passage-Food-Act\\_FINAL2.pdf](http://www.makeourfoodsafes.org/tools/assets/files/APHA_Senate-Passage-Food-Act_FINAL2.pdf)

<sup>2</sup> NHTSA's vehicle safety standards have reduced the traffic fatality rate from nearly 3.5 fatalities per 100 million vehicles traveled in 1980 to 1.41 fatalities per 100 million vehicles traveled in 2006. Steinzor, R., & Shapiro, S. (2010). *The People's Agents and the Battle to Protect the American Public: Special Interests, Government, and Threats to Health, Safety, and the Environment*: University of Chicago Press.

<sup>3</sup> Clean Air Act rules saved 164,300 adult lives in 2010. In February 2011, EPA estimated that by 2020 they will save 237,000 lives annually. EPA air pollution controls saved 13 million days of lost work and 3.2 million days of lost school in 2010, and EPA estimates that they will save 17 million work-loss days and 5.4 million school-loss days annually by 2020. See U.S. Environmental Protection Agency, Office of Air and Radiation. (2011, March). *The Benefits and Costs of the Clean Air and Radiation Act from 1990 to 2020*. Available from: <http://www.epa.gov/oar/sect812/feb11/fullreport.pdf>.

<sup>4</sup> EPA regulations phasing out lead in gasoline helped reduce the average blood lead level in U.S. children ages 1 to 5. During the years 1976 to 1980, 88 percent of all U.S. children had blood levels in excess of 10µg/dL; during the years 1991 to 1994, only 4.4 percent of all U.S. children had blood levels in excess of that dangerous amount. Office of Management and Budget, Office of Information and Regulatory Affairs. (2011). *2011 Report to Congress on the Benefits and Costs of Federal Regulations on Unfunded Mandates on State, Local, and Tribal Entities*. Available from: [http://www.whitehouse.gov/sites/default/files/omb/inforeg/2011\\_cb/2011\\_cba\\_report.pdf](http://www.whitehouse.gov/sites/default/files/omb/inforeg/2011_cb/2011_cba_report.pdf).

<sup>5</sup> National Council on Disability. (2007). *The Impact of the Americans with Disabilities Act*. Available from: <http://www.ncd.gov/publications/2007/07262007>.

<sup>6</sup> There are important exceptions to the child labor prohibition; significant enforcement failures regarding the minimum wage, child labor and length of work week (before time and a half compensation is mandated). But the

- Saved the lives of thousands of workers every year.<sup>7</sup>
- Saved consumers and taxpayers billions of dollars by facilitating generic competition for medicines.<sup>8</sup>
- Protected the elderly and vulnerable consumers from a wide array of unfair and deceptive advertising techniques.<sup>9</sup>
- For half a century in the mid-twentieth century, and until the onset of financial deregulation, provided financial stability and a right-sized financial sector, helping create the conditions for robust economic growth and shared prosperity.<sup>10</sup>

These are not just the achievements of a bygone era. Regulation continues to improve the quality of life for every American, every day. Ongoing and emerging problems and a rapidly changing economy require the issuance of new rules to ensure that America is strong and safe, healthy and wealthy. Consider a small sampling of rules recently issued, pending, or that are or should be under consideration:

- **Fuel efficiency standards.** Pursuant to the Energy Policy and Conservation Act, the Energy Independence and Security Act and the Clean Air Act, the National Highway Safety and Transportation Agency and the Environmental Protection Agency have proposed new automobile and vehicular fuel efficiency standards. The new rules, on an average industry fleet-wide basis for cars and trucks combined, establish standards of 40.1 miles per gallon (mpg) in model year 2021, and 49.6 mpg in model year 2025. The agencies estimate that fuel savings will far outweigh higher vehicle costs, and that the net benefits to society from 2017-2025 will be in the range of \$311 billion to \$421 billion. The auto industry was integrally involved in the development of these proposed standards, and supports their promulgation.
- **Food safety rules.** In 2010, with support from both industry and consumer groups, and in response to a series of food contamination incidents that rocked the nation, Congress passed the Food Safety Modernization Act. The Act should improve the safety of eggs,

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quality of improvement in American lives has nonetheless been dramatic. Lardner, J. (2011). *Good Rules: 10 Stories of Successful Regulation*. Demos. Available from:

<[http://www.demos.org/sites/default/files/publications/goodrules\\_1\\_11.pdf](http://www.demos.org/sites/default/files/publications/goodrules_1_11.pdf)>.

<sup>7</sup> Deaths on the job have declined from more than 14,000 per year in 1970, when the Occupational Safety and Health Administration was created to under 4,500 at present. See AFL-CIO. (2015, April.) *Death on the Job: The Toll of Neglect*, p. 1. Available from:

<<http://www.aflcio.org/content/download/154671/3868441/DOJ2015Finalnbug.pdf>>. Mining deaths fell by half shortly after creation of the Mine Safety and Health Administration. Weeks, J. L., & Fox, M. (1983). Fatality rates and regulatory policies in bituminous coal mining, United States, 1959-1981. *American journal of public health*, 73(11), 1278.

<sup>8</sup> Through regulations facilitating effective implementation of the Drug Price Competition and Patent Term Restoration Act of 1984 ("Hatch-Waxman"), including by limiting the ability of brand-name pharmaceutical companies to extend and maintain government-granted monopolies. Troy, D. E. (2003). *Drug Price Competition and Patent Term Restoration Act of 1984 (Hatch-Waxman Amendments)*. Statement before the Senate Committee on the Judiciary. Available from: <<http://www.fda.gov/newsevents/testimony/ucm115033.htm>>.

<sup>9</sup> See 16 CFR 410-460.

<sup>10</sup> See Stiglitz, J. E. (2010). *Freefall: America, free markets, and the sinking of the world economy*: WW Norton & Co Inc.; Kuttner, R. (2008). *The Squandering of America: how the failure of our politics undermines our prosperity*: Vintage.

dairy, seafood, fruits, vegetable and many processed and imported foods, but its effective implementation depends on rulemaking. Not so incidentally, food contamination incidents have major harmful economic impact on the agriculture and food industries and job creation and preservation in those industries.

- **Energy efficiency standards.** Pursuant to the Energy Security and Independence Act, the Department of Energy has proposed energy efficiency standards for a range of products, including Metal Halide Lamp Fixtures, Commercial Refrigeration Equipment, and Battery Chargers and External Power Supplies, Walk-In Coolers and Walk-In Freezers, Residential Clothes Washers.<sup>11</sup> The Department of Energy estimates the net savings from implementation of the Energy Security and Independence Act to be \$48 billion - \$105 billion (in 2007 dollars).<sup>12</sup>
- **Rules to avert workplace hazards.** By way of example, consider the case of beryllium, a toxic substance to which workers in the electronics, nuclear, and metalwork sector are exposed. The current OSHA beryllium standard, based on science from the 1950s, allows workers to be exposed at levels that are ten times higher than those allowed by Department of Energy for nuclear power plant workers. Public Citizen petitioned OSHA to update the standard in 2001. In response, the agency began a rulemaking in November 2002. It is a testament to major problems in the regulatory process that OSHA has still not issued appropriate rules. Issuance of a rule could avert thousands of cases of serious disease.<sup>13</sup>
- **Controls on Wall Street.** As discussed in more detail below, the 2008 financial crash was a direct result of regulatory failures. These failures including inadequate regulation of mortgages and other consumer financial products, on the one hand, and esoteric financial products and the markets on which they trade, on the other. Another critical failure was permitting the rise of too-big-to-fail financial institutions, traceable both to the failure to enforce existing rules and policies, and the repeal and nonissuance of important rules. Few people are entirely satisfied with the Dodd-Frank legislation—Public Citizen is highly critical of a number of important omissions—but the Act does include an array of very important reforms that will make our financial system fairer and more stable—if properly implemented through robust rulemaking.

Among many other important provisions are crucial consumer protections. Dodd-Frank created the Consumer Financial Protection Bureau, charging the agency with the single mission of protecting consumers and empowering it to issue new consumer protection rules. Given the very considerable extent to which the financial industry has constructed a business model around trickery and unjust fees, CFPB rulemaking can afford consumer dramatic benefits. Such rules may concern matters including: requiring mortgage lenders

<sup>11</sup> List of Regulatory Actions Currently Under Review. Available from: <<http://www.reginfo.gov/public/jsp/EO/eoDashboard.jsp>>.

<sup>12</sup> U.S. Department of Energy. (2007). *Energy Independence and Security Act of 2007 Prescribed Standards*. Available from: <[http://www1.eere.energy.gov/buildings/appliance\\_standards/m/eisa2007.html](http://www1.eere.energy.gov/buildings/appliance_standards/m/eisa2007.html)>.

<sup>13</sup> U.S. Occupational Safety and Health Administration. (2007). *Preliminary Initial Regulatory Flexibility Analysis of the Preliminary Draft Standard for Occupational Exposure to Beryllium*.

to consider borrowers' ability to pay; prohibiting banks from charging excessive overdraft fees or tricking consumers into opting in to unreasonable overdraft fee harvesting schemes; eliminating forced arbitration provisions in consumer financial contracts; banning unfair practices in the payday loan industry; prohibiting kickbacks to auto dealers who steer buyers into overpriced loans; stopping student loan companies from tricking students into taking high-priced private loans before they exhaust cheaper federal loans.<sup>14</sup>

- **Generic competition for biotech medicines.** An overlooked component of the Affordable Care Act was the creation of a process for the Food and Drug Administration to grant regulatory approval for generic biologic pharmaceutical products—essentially generic versions of biotech medicines. Because the molecular composition of biologic drugs is more complicated than traditional medicines, FDA had adopted the position that, with some exceptions, it could not grant regulatory approval for biologics under its previously existing authority. In an important provision of the Affordable Care Act—supported by the biotech industry—FDA was explicitly granted such authority. The provision wrongly grants extended monopolies to brand-name biologic manufacturers, but belated generic competition is better than none. Implementation of the new regulatory pathway for biogenerics, however, depends on issuance of rules by the FDA. Biogeneric competition will save consumers and the government billions of dollars annually.
- **Crib safety.** Pursuant to the Consumer Product Safety Improvement Act of 2008, the Consumer Product Safety Commission (CPSC) finalized updated safety standards for cribs that halted the manufacture and sale of traditional drop-side cribs, required stronger mattress supports, more durable hardware and regular safety testing. These new crib safety standards mean "that parents, grandparents, and caregivers can now shop for cribs with more confidence—confidence that the rules put the safety of infants above all else."<sup>15</sup>
- **The Physician Payment Sunshine Act.** This component of the Affordable Care Act requires the disclosure of payments and gifts by pharmaceutical and medical device companies to physicians and hospitals. The mere fact of disclosure is expected to curtail the improper influence of industry over research, education and clinical decision making. Putting the Act into place required implementing rules.<sup>16</sup>

Although most regulations do not have economic objectives as their primary purpose, in fact regulation is overwhelmingly positive for the economy. It is worth underscoring this point, because concerns about particular rules or that the rulemaking process is unfair to regulated industry are usually rooted in economic arguments.

<sup>14</sup> National Consumer Law Center. (2010). *An Agenda for the Consumer Financial Protection Bureau: Challenges for a New Era in Consumer Protection*. Retrieved 24 February, 2012, Available from: <[http://www.nclc.org/images/pdf/regulatory\\_reform/pr-cfpb-agenda.pdf](http://www.nclc.org/images/pdf/regulatory_reform/pr-cfpb-agenda.pdf)>

<sup>15</sup> Consumer Federation of America. (2011, June 28). *Senators, CPSC, Consumer Advocates Applaud Strong Crib Safety Standards to Prevent Infant Deaths and Injuries*. Available from: <<http://www.consumerfed.org/pdfs/crib-standards-press-release-6-28-11.pdf>>.

<sup>16</sup> 42 CFR Parts 402 and 403. February 8, 2013.

While regulators commonly do not have economic growth and job creation as a mission priority, they are mindful of regulatory cost, and by statutory directive or on their own initiative typically seek to minimize costs; relatedly, the rulemaking process gives affected industries ample opportunity to communicate with regulators over cost concerns, and these concerns are taken into account. To review the regulations actually proposed and adopted is to see how much attention regulators pay to reducing cost and detrimental impact on employment. And to assess the very extended rulemaking process is to see how substantial industry influence is over the rules ultimately adopted—or discarded.

There is a large body of theoretical and non-empirical work on the cost of regulation, some of which yields utterly implausible cost estimates. There is also a long history of business complaining about the cost of regulation—and predicting that the next regulation will impose unbearable burdens. More informative than the theoretical work, anecdotes and allegations is a review of the actual costs and benefits of regulations, though even this methodology is significantly imprecise and heavily biased against the benefits of regulation. Every year, the Office of Management and Budget (OMB) analyzes the costs and benefits of rules with significant economic impact. The benefits massively exceed costs.

The principle finding of OMB's draft 2015 Report to Congress on the Benefits and Costs of Federal Regulation is:

The estimated annual benefits of major Federal regulations reviewed by OMB from October 1, 2004, to September 30, 2014, for which agencies estimated and monetized both benefits and costs, are in the aggregate between \$216 billion and \$812 billion, while the estimated annual costs are in the aggregate between \$57 billion and \$85 billion. These ranges are reported in 2001 dollars and reflect uncertainty in the benefits and costs of each rule at the time that it was evaluated.<sup>17</sup>

In other words, even by OMB's most conservative accounting, the benefits of major regulations over the last decade exceeded costs by a factor of more than two-to-one. And benefits may exceed costs by a factor of 15.

These results are consistent year-to-year as the following table shows.

<sup>17</sup> Office of Management and Budget, Office of Information and Regulatory Affairs. (2015). Draft 2015 Report to Congress on the Benefits and Costs of Federal Regulations on Unfunded Mandates on State, Local, and Tribal Entities. pp. 1-2. Available at: [https://www.whitehouse.gov/sites/default/files/omb/inforeg/2015\\_cb/draft\\_2015\\_cost\\_benefit\\_report.pdf](https://www.whitehouse.gov/sites/default/files/omb/inforeg/2015_cb/draft_2015_cost_benefit_report.pdf).

**Total Annual Benefits and Costs of Major Rules by Fiscal Year (billions of 2001 dollars)<sup>18</sup>**

<b>Fiscal Year</b>	<b>Number of Rules</b>	<b>Benefits</b>	<b>Costs</b>
2001	12	22.5 to 27.8	9.9
2002	2	1.5 to 6.4	0.6 to 2.2
2003	6	1.6 to 4.5	1.9 to 2.0
2004	10	8.8 to 69.8	3.0 to 3.2
2005	12	27.9 to 178.1	4.3 to 6.2
2006	7	2.5 to 5.0	1.1 to 1.4
2007	12	28.6 to 184.2	9.4 to 10.7
2008	11	8.6 to 39.4	7.9 to 9.2
2009	15	8.6 to 28.9	3.7 to 9.5
2010	18	18.6 to 85.9	6.4 to 12.4
2011	13	34.3 to 98.5	5.0 to 10.2
2012	14	53.2 to 114.6	14.8 to 19.5
2013	7	25.6 to 67.3	2.0 to 2.5
2014	13	8.1 to 18.9	2.5 to 3.7

The reason for the consistency is that regulators pay a great deal of concern to comparative costs and benefits (even though there is, we believe, a built-in bias of formal cost-benefit analysis against regulatory initiative<sup>19</sup>; see further comments below). Very few major rules are adopted where projected costs exceed projected benefits, and those very few cases—one of which is the Congressional mandate for railroads to adopt Positive Train Controls, a technology that would have averted the recent Amtrak accident—typically involve direct Congressional mandates.

It should also be noted that relatively high regulatory compliance costs, as discussed further below, do not necessarily have negative job impacts; firm expenditures on regulatory compliance typically create new jobs within affected firms or other service or product companies with which they contract.

Moreover, the empirical evidence also fails to support claims that regulation causes significant job loss. Insufficient demand is the primary reason for layoffs. In extensive survey data collected by the Bureau of Labor Statistics, employers cite lack of demand roughly 100 times more

<sup>18</sup> Office of Management and Budget, Office of Information and Regulatory Affairs. (2015). *Draft 2015 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities. Table 1-4*, pp. 20-21. Available at:

[https://www.whitehouse.gov/sites/default/files/omb/inforeg/2015\\_cb/draft\\_2015\\_cost\\_benefit\\_report.pdf](https://www.whitehouse.gov/sites/default/files/omb/inforeg/2015_cb/draft_2015_cost_benefit_report.pdf); 2001-2004 data from: Office of Management and Budget, Office of Information and Regulatory Affairs. (2011). *2011 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities. Table 1-3*, p. 19-20. Available at:

[http://www.whitehouse.gov/sites/default/files/omb/inforeg/2011\\_cb/2011\\_cba\\_report.pdf](http://www.whitehouse.gov/sites/default/files/omb/inforeg/2011_cb/2011_cba_report.pdf).

<sup>19</sup> See, e.g., Shapiro, S. et al., *CPR Comments on Draft 2010 Report to Congress on the Benefits and Costs of Federal Regulations* 16-19 (App. A, Pt. C.) (2010), Available from: <[http://www.progressivereform.org/articles/2010\\_CPR\\_Comments\\_OMB\\_Report.pdf](http://www.progressivereform.org/articles/2010_CPR_Comments_OMB_Report.pdf)>; Steinzor, R. et al., *CPR Comments on Draft 2009 Report to Congress on the Benefits and Costs of Federal Regulations* 16-19 (App. A, Pt. C.) (2009), Available from: <[http://www.progressivereform.org/articles/2009\\_CPR\\_Comments\\_OMB\\_Report.pdf](http://www.progressivereform.org/articles/2009_CPR_Comments_OMB_Report.pdf)>.



frequently than government regulation as the reason for mass layoffs!<sup>20</sup> (Unfortunately, in response to budget cuts, the BLS ceased producing its mass layoff report in 2013.)

**Reason for layoff: 2008-2012<sup>21</sup>**

	2008	2009	2010	2011	2012
<b>Business Demand</b>	516,919	824,834	384,564	366,629	461,328
<b>Governmental regulations/intervention</b>	5,505	4,854	2,971	2,736	3,300

It is also the case that firms typically innovate creatively and quickly to meet new regulatory requirements, even when they fought hard against adoption of the rules.<sup>22</sup> The result is that costs are commonly lower than anticipated.

**B. Job-destroying regulatory failure and the Great Recession**

Missing from much of the current policy debate on jobs and regulation is a crucial, overriding fact: The Great Recession and the ongoing weak jobs market and national economy are a direct result of too little regulation and too little regulatory enforcement.

A very considerable literature, and a very extensive Congressional hearing record, documents in granular detail the ways in which regulatory failure led to financial crash and the onset of the Great Recession. “Widespread failures in financial regulation and supervision proved devastating to the stability of the nation’s financial markets,” concluded the Financial Crisis Inquiry Commission.<sup>23</sup> “Deregulation went beyond dismantling regulations,” notes the Financial Crisis Inquiry Commission. “[I]ts supporters were also disinclined to adopt new regulations or challenge industry on the risks of innovations.”<sup>24</sup>

The regulatory failures were pervasive, the Financial Crisis Inquiry Commission concluded:

<sup>20</sup> U.S. Department of Labor, Bureau of Labor Statistics. (2012, November). *Extended Mass Layoffs in 2011. Table 5. Reason for layoff: extended mass layoff events, separations, and initial claimants for unemployment insurance, private nonfarm sector, 2009-2011*. Available from: <<http://www.bls.gov/mls/mlsreport1039.pdf>>.

<sup>21</sup> U.S. Department of Labor, Bureau of Labor Statistics. (2012, November). *Extended Mass Layoffs in 2011. Table 5. Reason for layoff: extended mass layoff events, separations, and initial claimants for unemployment insurance, private nonfarm sector, 2010-2012*. Available from: <<http://www.bls.gov/mls/mlsreport1043.pdf>>. U.S. Department of Labor, Bureau of Labor Statistics. (2013, September). *Extended Mass Layoffs in 2011. Table 4. Reason for layoff: extended mass layoff events, separations, and initial claimants for unemployment insurance, private nonfarm sector, 2009-2011*. Available from: <<http://www.bls.gov/mls/mlsreport1039.pdf>>; U.S. Department of Labor, Bureau of Labor Statistics. (2011, November). *Extended Mass Layoffs in 2010. Table 6. Reason for layoff: extended mass layoff events, separations, and initial claimants for unemployment insurance, private nonfarm sector, 2008-2010*. Available from: <<http://www.bls.gov/mls/mlsreport1038.pdf>>.

<sup>22</sup> Mouzoon, N., & Lincoln, T. (2011). *Regulation: The Unsung Hero in American Innovation*. Public Citizen. Available from: <<http://www.citizen.org/documents/regulation-innovation.pdf>>.

<sup>23</sup> Financial Crisis Inquiry Commission. (2011). *The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States*. Washington, D.C.: Government Printing Office. p. 30.

<sup>24</sup> *The Financial Crisis Inquiry Report*. p. 53.

The sentries were not at their posts, in no small part due to the widely accepted faith in the self-correcting nature of the markets and the ability of financial institutions to effectively police themselves. More than 30 years of deregulation and reliance on self-regulation by financial institutions, championed by former Federal Reserve Chairman Alan Greenspan and others, supported by successive administrations and Congresses, and actively pushed by the powerful financial industry at every turn, had stripped away key safeguards, which could have helped avoid catastrophe. This approach had opened up gaps in oversight of critical areas with trillions of dollars at risk, such as the shadow banking system and over-the-counter derivatives markets. In addition, the government permitted financial firms to pick their preferred regulators in what became a race to the weakest supervisor.

The regulatory failure story can perhaps be summarized as follows: Financial deregulation and non-regulation created a vicious cycle that helped inflate the housing bubble and an interconnected financial bubble. Weak mortgage regulation enabled the spread of toxic and predatory mortgages that helped fuel the housing bubble. Deregulated Wall Street firms and big banks exhibited an insatiable appetite for mortgage loans, irrespective of quality, thanks to insufficiently regulated securitization, off-the-books accounting, the spread of shadow banking techniques, dangerous compensation incentives and inadequate capital standards. Reckless financial practices were ratified by credit ratings firms, paving the way for institutional funders to pour billions into mortgage-related markets; and an unregulated derivatives trade offered the illusion of systemic insurance but actually exacerbated the crisis when the housing bubble popped and Wall Street crashed.

The costs of this set of regulatory failures are staggeringly high, and far outdistance any plausible story about the "cost" of regulation.

To prevent the collapse of the financial system, the federal government provided incomprehensibly huge financial supports, far beyond the \$700 billion in the much-maligned Troubled Assets Relief Program (TARP). The Special Inspector General for the Troubled Assets Relief Program (SIGTARP) estimated that "though a huge sum in its own right, the \$700 billion in TARP funding represents only a portion of a much larger sum—estimated to be as large as \$23.7 trillion—of potential Federal Government support to the financial system."<sup>25</sup> Much of this sum was never allocated, and most of the TARP funds were paid back. However, the regulatory reform policy debate should acknowledge that such unfathomable sums were put at risk thanks to regulatory failure.

Even more significant, however, are the actual losses traceable to the regulatory failure-enabled Great Recession. These losses are real, not potential; they are at a comparable scale of more than \$20 trillion; they involve an actual loss of economic output, not just a reallocation of resources; and they have imposed devastating pain on families, communities and national well-being.

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<sup>25</sup> Special Inspector General for the Troubled Assets Relief Program (SIGTARP) (2009, July 21.) Quarterly Report to Congress. p. 129. Available from: [http://www.sigtar.gov/Quarterly%20Reports/July2009\\_Quarterly\\_Report\\_to\\_Congress.pdf](http://www.sigtar.gov/Quarterly%20Reports/July2009_Quarterly_Report_to_Congress.pdf).

A GAO study found that "[t]he 2007-2009 financial crisis, like past financial crises, was associated with not only a steep decline in output but also the most severe economic downturn since the Great Depression of the 1930s."<sup>26</sup> Reviewing estimates of lost economic output, GAO reported that the present value of cumulative output losses could exceed \$13 trillion.<sup>27</sup> Additionally, GAO found that "households collectively lost about \$9.1 trillion (in constant 2011 dollars) in national home equity between 2005 and 2011, in part because of the decline in home prices."<sup>28</sup>

The recession threw millions out of work, and left millions still jobless or underemployed. "The monthly unemployment rate peaked at around 10 percent in October 2009 and remained above 8 percent for over 3 years, making this the longest stretch of unemployment above 8 percent in the United States since the Great Depression," GAO noted.<sup>29</sup>

The economic impact on families is crushing, even leaving aside social and psychological consequences. "Displaced workers—those who permanently lose their jobs through no fault of their own—often suffer an initial decline in earnings and also can suffer longer-term losses in earnings," reports GAO. For example, one study found that workers displaced during the 1982 recession earned 20 percent less, on average, than their non-displaced peers 15 to 20 years later.<sup>30</sup> Thanks to lost income and especially collapsed housing prices, families have seen their net worth plummet. According to the Federal Reserve's Survey of Consumer Finances, median household net worth fell by \$49,100 per family, or by nearly 39 percent, between 2007 and 2010.<sup>31</sup>

The foreclosure crisis stemming from the toxic brew of collapsing housing prices, exploding and other unsustainable mortgages and high unemployment has devastated families and communities across the nation.<sup>32</sup>

The financial crash and Great Recession is also, not so incidentally, the primary explanation for historically high federal deficits. Reports GAO:

From the end of 2007 to the end of 2010, federal debt held by the public increased from roughly 36 percent of GDP to roughly 62 percent. Key factors contributing to increased deficit and debt levels following the crisis included (1) reduced tax revenues, in part

<sup>26</sup> U.S. Government Accountability Office. (2013, Jan. 13). *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. p. 12. Available from: <<http://www.gao.gov/products/GAO-13-180>>.

<sup>27</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. p. 16.

<sup>28</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. p. 21. There is necessarily a significant amount of uncertainty around such analyses. Other estimates have placed the loss somewhat lower. A recent Congressional Budget Office study estimates the cumulative loss from the recession and slow recovery at \$5.7 trillion." (Congressional Budget Office. 2012. *The Budget and Economic Outlook: Fiscal Years 2012 to 2022*. p. 26.) One complicating issue is determining which losses should be attributed to the recession and which to other issues. For example, GAO notes, "analyzing the peak-to-trough changes in certain measures, such as home prices, can overstate the impacts associated with the crisis, as valuations before the crisis may have been inflated and unsustainable."<sup>29</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. p. 17.

<sup>29</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. pp. 17-18.

<sup>30</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. pp. 18-19.

<sup>31</sup> Cited in *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. p. 16.

<sup>32</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. pp. 23-24.

driven by declines in taxable income for consumers and businesses; (2) increased spending on unemployment insurance and other nondiscretionary programs that provide assistance to individuals impacted by the recession; (3) fiscal stimulus programs enacted by Congress to mitigate the recession, such as the American Recovery and Reinvestment Act of 2009 (Recovery Act); and (4) increased government assistance to stabilize financial institutions and markets.<sup>33</sup>

It should be noted that there are, to be sure, dissenting views to narratives that place regulatory failure at the core of the explanation for the Great Recession and financial crisis. Perhaps the most eloquent version of this dissent is contained in the primary dissenting statement to the Financial Crisis Inquiry Commission.

The dissent explained that "we ... reject as too simplistic the hypothesis that too little regulation caused the Crisis,"<sup>34</sup> arguing that the *amount* of regulation is an imprecise and perhaps irrelevant metric. This is a reasonable position (and it applies equally to those who complain about "too much" regulation); what matters is the quality of regulation—both the rules and standards of enforcement.

The FCIC dissent began its explanation for the financial crisis with the creation of a credit bubble and a housing bubble, which it argued laid the groundwork for a financial crisis thanks to a series of other, interconnected factors, including the spread of nontraditional mortgages, securitization, poor functioning by credit rating firms, inadequate capitalization by financial firms, the amplification of housing bets through use of synthetic credit derivatives, and the risk of contagion due to excessive interconnectedness.

However, to review this list is to see how the FCIC dissent also implicitly argued that the crisis can be blamed in large part on regulatory failure. For all of these factors should have been tamed by appropriate regulatory action.

## II. Homeland Security and Government Affairs Committee Hearing Case Study Examples

This hearing on the administrative process is focusing especially on three recent, high-profile rules: the Department of Labor's Retirement Advice Conflict of Interest Rule, the Federal Communications Commission's Net Neutrality Rule, and the Environmental Protection Agency and Army Corps of Engineers' Clean Water Rule. These rules have little in common, making it hard to draw from them important lessons about the rulemaking process. Each of them does advance important public policy objectives, however, illustrating the crucial importance of the regulatory process to improving the quality of life for Americans. Each of them also highlights the care with which agencies generally approach rulemaking, and the extensive consideration given to the views of regulated industry.

<sup>33</sup> *Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act*. p. 26.

<sup>34</sup> *The Financial Crisis Inquiry Report*. (Dissenting Views By Keith Hennessey, Douglas Holtz-Eakin, and Bill Thomas.) p. 414.

### **A. Preventing Conflicts of Interest in the Provision of Retirement Advice – the Fiduciary Rule**

More than five years in the making, the Department of Labor earlier this month adopted a final version of its rule to eliminate conflicts of interest among those who provide investment advice to retirement savers.<sup>35</sup> This crucial consumer protection rule is known as the “fiduciary rule” because clarifies the definition of what constitutes a “fiduciary” under the Employment Retirement Income Security Act of 1974 (ERISA). In short, the common-sense rule requires that retirement investor advisors must serve the best interests of their clients.

ERISA established the definition of a fiduciary adviser as anyone who “renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or property of such a plan, or any authority or responsibility to do so.” In implementing the law, the Department of Labor created a five-part test that must be met for an adviser to be considered a fiduciary under ERISA. This significantly narrowed the statutory definition and created loopholes that became highly problematic over time. Broker-dealers, insurance agents and other sales-based advisers have used these loopholes to provide retirement advice without abiding by a fiduciary standard. Their advice was required only to be “suitable.”

Over the last several decades, the nation has seen a massive shift from defined benefit pension plans to defined contribution retirement accounts, such as 401(k)s, as well as the rise of Individual Retirement Accounts (IRAs). Defined contribution account and IRA holders are in charge of their investments, and need investment advice. The narrow definition of fiduciary prior to adoption of the fiduciary rule meant that those providing that advice could permissibly maintain undisclosed conflicts of interest. Given the increasing complexity of financial products and markets, this created an opportunity for significant abuse.

The fiduciary rule aims to mitigate these conflicts of interest. Under the rule, any person compensated for making individualized recommendations to an IRA owner or pension plan participant is a fiduciary and must provide impartial advice in their client’s best interest.

It’s hard to overstate how common-sense is this measure. Consumers assuredly expect that professionals on whom they rely for advice will serve their best interests. For many, navigating the complexities of the market is intimidating and confusing. Even sophisticated consumers need assistance – that is why they are seeking advice – and assume that their advisors are serving their clients’ interests, not advancing the advisors’ financial interests at the expense of clients. Consumers generally have little knowledge and understanding of the various legal categories that determine the duty of loyalty owed them by advisors.<sup>36</sup> Proportionately, very few consumers understand the significance of high fees in reducing long-term yield – even those fees that are properly disclosed -- making consumers extraordinarily vulnerable to manipulation.<sup>37</sup> Yet, under

<sup>35</sup> Final Rule, Federal Register, Vol. 81, No. 68, April 8, 2016, 20946.

<sup>36</sup> Consumer Financial Protection Bureau, “Senior Designations for Financial Advisers,” April 18, 2013, available at: [http://files.consumerfinance.gov/f/201304\\_CFPB\\_OlderAmericans\\_Report.pdf](http://files.consumerfinance.gov/f/201304_CFPB_OlderAmericans_Report.pdf).

<sup>37</sup> See, for example, Kate Stalter, “The Investment Fees You Don’t Realize You’re Paying,” US News, December 15, 2014, available at: <http://money.usnews.com/money/personal-finance/mutual-funds/articles/2014/12/15/the-investment-fees-you-dont-realize-youre-paying>.

rules in place prior to adoption of the fiduciary rule, they were actually permitted to operate with conflicts of interest that did not have to be disclosed; give imprudent and disloyal advice; and steer IRA owners to investments based on their own, rather than the customers' best interest.<sup>38</sup>

Of course, many investment advisors even prior to adoption of the final rule operated to advance their clients' best interest. And, to be very clear, assuredly many of those who did not themselves serve their clients' best interest did not realize how conflicts alter the advice they give; the impact of conflicts of interest are often not apparent even to those conflicted.

Yet just as assuredly, conflicts have been rife and materially harming consumers. After a thorough review of the available literature, the Council of Economic Advisers determined that conflicts reduce investor returns to IRAs by 1 percent a year, or \$17 billion annually.<sup>39</sup> An individual consumer could easily retire with an investment account worth 20 percent less than it would otherwise be as a result of these expenses.<sup>40</sup>

The fiduciary rule will assure that investment advisers serve the best interests of their clients, and eliminate the conflicts that cost consumers so significantly.

Perhaps surprisingly, broker-dealers have objected to the new rule. While regulated entities commonly oppose the adoption of new rules that constrain abusive activity, it is still noteworthy that many in the industry have sought to prevent adoption of a standard that would require them to serve their clients' best interests. Predictably, those opposed to the fiduciary rule do not argue the merits of conflicts of interest. Instead, they contend that compliance costs will be excessively burdensome and might drive small firms out of business. Neither claim stands up under scrutiny. The Department of Labor's careful and detailed cost estimate – based significantly on data provided by industry -- place compliance costs at between \$3.3 billion and \$3.6 billion.<sup>41</sup> While industry has stated publicly that compliance costs threaten business viability, leading companies are making contrary claims to their own investors. Referring to statements the companies have made in their Securities and Exchange Commission filings, Senator Elizabeth Warren and Representative Elijah Cummings write, "In contrast to their public doomsday predictions, industry leaders have told their own investors that they don't see this as a significant hurdle," "will once again respond to marketplace or regulatory changes effectively," and that they are well-positioned to adapt to any regulatory framework that emerges."<sup>42</sup> Meanwhile, large and small firms can continue to profitably serve small investors with affordable advice that's in their

<sup>38</sup> Final Rule, Federal Register, Vol. 81, No. 68, April 8, 2016, 20946.

<sup>39</sup> Council of Economic Advisers, The Effects of Conflicted Investment Advice on Retirement Savings, February 2015, available at: [https://www.whitehouse.gov/sites/default/files/docs/cea\\_coi\\_report\\_final.pdf](https://www.whitehouse.gov/sites/default/files/docs/cea_coi_report_final.pdf).

<sup>40</sup> Council of Economic Advisers, The Effects of Conflicted Investment Advice on Retirement Savings, February 2015, available at: [https://www.whitehouse.gov/sites/default/files/docs/cea\\_coi\\_report\\_final.pdf](https://www.whitehouse.gov/sites/default/files/docs/cea_coi_report_final.pdf).

<sup>41</sup> Department of Labor, "Regulating Advice Markets," April 2016, available at: <http://www.dol.gov/ebsa/pdf/conflict-of-interest-ria.pdf>.

<sup>42</sup> Senator Elizabeth Warren and Representative Elijah Cummings, Letter to Secretary of Labor Thomas Perez and Office of Management and Budget Director Shaun Donovan, February 11, 2015, available at: [http://www.warren.senate.gov/files/documents/2016-2-11\\_Letter\\_to\\_DOL\\_and\\_OMB.pdf](http://www.warren.senate.gov/files/documents/2016-2-11_Letter_to_DOL_and_OMB.pdf).

best interest according to a wide variety of business models, including those that charge commissions, as an increasing number are starting to do in anticipation of the rule.<sup>43</sup>

The fiduciary rule is the product of more than five years of work. First proposed in 2010, the Department withdrew its initial proposal to address concerns that were raised. Although it aimed to reintroduce the rule in early 2012, the next iteration was not proposed until 2015. During the prolonged period of delay until it proposed the revised rule in April 2015, the Department consulted extensively, including with stakeholders and other government agencies, particularly the Securities and Exchange Commission and the Financial Industry Regulatory Authority (FINRA).<sup>44</sup> The revised proposal was sent to the Office of Information and Regulatory Affairs (OIRA) for review in February 2015. OIRA held 21 stakeholder meetings on the issue before releasing the proposal, including with Fidelity Investments, the Financial Services Roundtable, and the U.S. Chamber of Commerce.<sup>45</sup>

On April 20, 2015, the Labor Department issued its updated proposal. After receiving requests for additional time to submit input on the revised rule, the Labor Department extended the comment period by two weeks in July and held a four-day hearing during the week of August 10, 2015. The Department then re-opened the comment period again for an additional two weeks for additional public testimony and comments. In total, there were over 100 days for the public to comment on the draft rule. The Department received 3,134 total comments, including 30 petitions that encompass an additional 386,889 comments.

The public participation in the process was dominated by investment and insurance industry firms and lobbyists as compared to public interest or consumer groups, and the final rule incorporates substantial revisions in response to comments received, intended especially to reduce compliance costs.<sup>46</sup>

The Committee majority has issued a report raising concerns about inter-agency disagreements over the fiduciary rule. But there is no question as to the Department of Labor's jurisdiction over the matters covered by the fiduciary rule; and disagreements among staff are to be expected and are an important part of the deliberative process. The final fiduciary rule is a long overdue measure, needlessly delayed for years, to adopt commonsense protections for consumers. It will, conservatively, save consumers \$17 billion every year, and materially advance the well-being of people in their retirement years. This is how regulation is supposed to work – albeit it should work more quickly.

<sup>43</sup> Michael Wursthorn, "Brokerages Adapt to Pending Labor Rule," Wall Street Journal, March 16, 2016, available at: [www.wsj.com/articles/brokerages-adapt-to-pending-labor-rule-1458151260](http://www.wsj.com/articles/brokerages-adapt-to-pending-labor-rule-1458151260); Jason Zweig, "Saving for Retirement? The Rulebook is About to Change," Wall Street Journal, April 4, 2016, available at: <http://www.wsj.com/articles/new-government-rule-rewrites-retirement-savings-1459762202>.

<sup>44</sup> See Appendix to Senate Homeland Security and Government Affairs Committee, Majority Report, "The Labor Department's Fiduciary Rule: How a Flawed Process Could Hurt Retirement Savers," (2016).

<sup>45</sup> EO 12,866 Meetings (2015) available at [www.reginfo.gov](http://www.reginfo.gov).

<sup>46</sup> Department of Labor, "Regulating Advice Markets," April 2016, available at: <http://www.dol.gov/ebsa/pdf/conflict-of-interest-ria.pdf>.

## B. Net Neutrality

The Federal Communication Commission's (FCC's) Open Internet ("Net Neutrality") order, adopted last year, is one of the most important developments in protecting consumers' access to a free and open internet.

In February 2015, the FCC voted to reclassify broadband internet service as a telecommunications service and adopt rules requiring Network Neutrality. The order followed years of contentious debate and extensive litigation, including over the FCC's jurisdictional authority. The jurisdictional issues were resolved by the agency's decision to classify broadband as a telecommunications service; and the Net Neutrality rules finally resolve crucial questions about the degree to which Internet Service Providers (ISPs) could control the flow of content over the Internet.

The rule establishes three bright line rules to protect a free and open Internet:

- No Blocking: broadband providers may not block access to legal content, applications, services, or non-harmful devices.
- No Throttling: broadband providers may not impair or degrade lawful internet traffic on the basis of content, applications, services, or non-harmful devices.
- No Paid Prioritization: broadband providers may not favor some lawful internet traffic over other lawful traffic in exchange for consideration of any kind—in other words, no "fast lanes." This rule also bans ISPs from prioritizing content and services of their affiliates.<sup>47</sup>

Policymakers of all stripes should celebrate the adoption of the Net Neutrality rule. It protects consumers, both from excessive tolls that could significantly impact their pocketbook, a diminished internet that would impose costs by diminishing their user experience<sup>48</sup> and, even more importantly, from ISP censorship or undue influence over what they could see. It advances core First Amendment values, ensuring that all lawful speech is treated equally on the Internet, made available without the censoring hand of a corporate Big Brother.<sup>49</sup> Without the Net Neutrality rule, ISPs might have blocked or interfered with consumer access to information that they disfavored, or which is promulgated by speakers with limited financial backing and limited ability to pay ISP-imposed tolls. And, equally as significantly, the Net Neutrality promotes competition and innovation, preventing the ISPs controlling – and slowing – the innovation that is occurring across Internet platforms.<sup>50</sup>

<sup>47</sup> Federal Communications Commission, "Open Internet," available at: <https://www.fcc.gov/general/open-internet>.

<sup>48</sup> J. Scott Holladay, A.J. Glusman, Steven Soloway, "Internet Benefits," October 3, 2011, available at: <http://policyintegrity.org/publications/detail/internet-benefits1>.

<sup>49</sup> Jay Stanley, "Network Neutrality 101," American Civil Liberties Union, October 2010, available at: <https://www.aclu.org/report/network-neutrality-101-why-government-must-act-preserve-free-and-open-internet?redirect=free-speech-technology-and-liberty/network-neutrality-101-why-government-must-act-preserve-free-and-> ("Network neutrality is a consumer issue, but it is also one of the foremost free speech issues of our time.")

<sup>50</sup> Digital Media Association, "Competition and Net Neutrality," available at: <http://www.digmedia.org/issues-and-policy/net-neutrality>.



Viewed properly, the Net Neutrality rule is fundamentally a pro-market and pro-business<sup>51</sup> rule. It removes not government control, but corporate goliath ISP gatekeepers that, in the absence of the rule, could stifle market competition and consumer freedom and liberty.

The opposition to the rule came from a powerful vested interest, the broadband ISPs, but one year's time has already dispelled their claims that the rule would impose catastrophic costs on them. In fact, analysts have found that the "Profits and profit margins are at historic, monopoly-like levels, and they continue to grow as ISPs exercise market power in an increasingly uncompetitive market." Broadband ISPs are increasing their capital investment as compared to the period before the rule, investing nearly \$3 billion in 2015. Revenues across the industry are up, with 2015 revenues \$22 billion above the previous year. Stock values have also increased.<sup>52</sup>

The Net Neutrality rule ranks close to the top of the highest-profile rulemakings in history. It is the product of a very lengthy FCC process and extensive litigation. One may or may not like the outcome – though the decision looks increasingly positive as time passes and promised harms do not materialize – but it is hard to argue the agency did not thoroughly vet the issue and engage the public.

Following several legal battles that demonstrated the need for the FCC to clarify that Net Neutrality principles – which have been long been the *de facto* standard of the internet – were binding commission standards, the FCC took its first steps toward the current Net Neutrality order in 2010 by proposing an Open Internet order.<sup>53</sup> This order was subsequently struck down by the DC Circuit Court of Appeals, but the court left open the possibility of the FCC issuing a statutorily justifiable Net Neutrality rule by reclassifying broadband services as "telecommunications services" under title II of the Communications Act.<sup>54</sup> In response, the FCC published a Notice of Proposed Rulemaking (NPRM) in May 2014 that fell short of adopting the reclassification of broadband services as "telecommunication services" but explicitly left open the possibility of doing so in the final rule.<sup>55</sup> After a robust public comment period that generated millions of public comments, the FCC released a final Report and Order in February 2015 that established strong net neutrality protections. The final order reclassified broadband services as telecommunications services; adopted Net Neutrality principles as binding rules; and invoked its discretion to forbear broadband providers from the vast majority of statutes and regulations that apply to regular telecommunication services.<sup>56</sup> That Order is currently being challenged in the DC Circuit Court of Appeals, although that court refused to stay the Order's enforcement pending a decision by the court.

<sup>51</sup> Alex Christensen, "4 Types of Businesses that Benefit from Net Neutrality," Global Risk Insights, March 10, 2015, available at: <http://globalriskinsights.com/2015/03/4-types-of-businesses-that-benefit-from-net-neutrality>.

<sup>52</sup> See Free Press, "Same As It Ever Was: The U.S. Broadband Market Continues to Thrive One Year After the FCC's Historic Network Neutrality Vote," March 7, 2016, available at: [http://www.freepress.net/sites/default/files/resources/free\\_press\\_broadband\\_market\\_one\\_year\\_later.pdf](http://www.freepress.net/sites/default/files/resources/free_press_broadband_market_one_year_later.pdf).

<sup>53</sup> Marguerite Reardon, "FCC Makes Net Neutrality Rules Official," CNet, December 21, 2010, available at: [www.cnet.com/news/fcc-makes-net-neutrality-rules-official](http://www.cnet.com/news/fcc-makes-net-neutrality-rules-official).

<sup>54</sup> *Verizon v. FCC*, January 14, 2014, available at:

[https://www.cadc.uscourts.gov/internet/opinions.nsf/3AF8B4D938CDEFA685257C6000532062/\\$file/11-1355-1474943.pdf](https://www.cadc.uscourts.gov/internet/opinions.nsf/3AF8B4D938CDEFA685257C6000532062/$file/11-1355-1474943.pdf).

<sup>55</sup> FCC, Protecting and Promoting the Open Internet NPRM, May 15, 2014, available at:

<https://www.fcc.gov/document/protecting-and-promoting-open-internet-nprm>.

<sup>56</sup> Final Order, <https://www.fcc.gov/document/fcc-releases-open-internet-order>.

The FCC's Net Neutrality rulemaking process was a true success in two respects. First, the agency received almost 4 million comments on the proposed rule through the public comment process (mostly in support of FCC's adoption of Net Neutrality).<sup>57</sup> This is the largest number of comments ever submitted in a federal rulemaking process—something that should be both celebrated and emulated. The notice and comment rulemaking process is predicated upon “democratizing” the way in which government agencies craft rules by encouraging broad and diverse participation from the public through submission of written comments. Done well, notice-and-comment provides a crucial way for government agencies to hear from the public and offsets the influence of powerful industries with developed channels of access into the government. Congressional efforts to reform the rulemaking process should seek to emulate the FCC's Net Neutrality success by focusing on maximizing public participation from as broad a variety of stakeholders as possible. Instead, it appears some in Congress are focusing instead on increasing the number of opportunities for public comment.<sup>58</sup> This approach does little to increase participation by a wide variety of stakeholders and further entrenches the current disparity between comments submitted by regulated industries as compared to average citizens in most rulemakings.<sup>59</sup> The solution is to make sure the government is hearing from as many voices as possible, not force the government to listen to the same voices even more times.

Second, the Net Neutrality rulemaking constituted an example of a government agency taking feedback from the public seriously, as is their legal requirement under the Administrative Procedure Act, and when appropriate making changes to their rules to respond to that feedback. It is the kind of responsiveness that should be celebrated by those who worry that public comments are ignored and notice-and-comment is meaningless because the outcome of the rulemaking is already pre-determined.

Some, including on this Committee, have contended that President Obama inappropriately influenced the FCC and pushed it to change its approach from the proposed rule to the final order.<sup>60</sup> These claims are misplaced. First, there is no evidence of any attempt to directly influence the FCC's rulemaking by the President or the White House. The President's public statement of support for a strong Net Neutrality rule is well within the President's authority and responsibility to make his policy views clear to the public. Agency independence does not mean the President cedes his First Amendment rights or duties to the public; it is not analogous to the need for walls between the White House and criminal investigators. And, indeed, past presidents have frequently made their policy preferences publicly known while FCC rulemakings were underway, sometimes in far more direct ways. For example, Presidents Ronald Reagan supported retaining financial syndication rules by the FCC which led the agency to withdraw its first

<sup>57</sup> Edward Wyatt, “Net Neutrality Comments to F.C.C. Overwhelmingly One-Sided, Study Say,” New York Times, September 18, 2014, available at: <http://bits.blogs.nytimes.com/2014/09/18/net-neutrality-comments-to-f-c-c-overwhelmingly-one-sided-study-says>

<sup>58</sup> See e.g. S. 1820, Early Participation In Regulations Act of 2015 (114<sup>th</sup> Congress) available at <https://www.congress.gov/bills/114/congress/senate-bill/1820>

<sup>59</sup> Wendy Wagner, Katherine Barnes & Lisa Peters, *Rulemaking in the Shade: Empirical Study of EPA's Toxic Emission Standards*, 63 Admin. L. Rev. 99, 125 (2011).

<sup>60</sup> Majority Staff Report, Committee on Homeland Security and Government Affairs, “Regulating the Internet,” February 29, 2016, available at: <http://www.hsgac.senate.gov/download/regulating-the-internet-how-the-white-house-bowled-over-fcc-independence>.

attempt at revising the financial syndication rules.<sup>61</sup> President George H.W. Bush then directed the agency to eliminate those same rules, which the agency subsequently did.<sup>62</sup> President Clinton also pushed the FCC to curtail advertising of hard liquor on TV, leading to a proposed rule by the FCC to do just that.<sup>63</sup> Finally, George W. Bush sent a personal letter to then FCC Chair Michael Powell asking him not to delay a commission vote on media ownership deregulation.<sup>64</sup> Powell then denied a request to delay the vote from fellow commissioners. Second, the President's proposal was substantially different from the FCC's final order in critical respects. The FCC's final order contained extensive forbearance for broadband providers from title II restrictions on telecommunications providers and applied title II to interconnection as well. Finally, there is ample evidence that FCC Chair Wheeler was undecided on key issues in the rulemaking and was considering a wide array of possible choices, including title II, well before President Obama's announcement.<sup>65</sup>

It is important to note that this Committee's concern about independent agencies being unduly influenced by the President, however unfounded and misplaced it is in this context, would in fact be exacerbated by legislation the Committee passed last October, namely the Independent Agency Regulatory Analysis Act (S. 1607). That bill would require independent agencies to send their significant proposed and final rules to the Office of Information and Regulatory Affairs (OIRA) for review and feedback as part of the public comment process. OIRA's regulatory review currently only extends to executive branch agencies that are subject to the Executive Orders authorizing OIRA's review functions. The inability for OIRA to review independent agency rulemakings is one of the key elements that maintain independent agencies' independence from the executive branch, along with restrictions on removals of independent agency heads by the President. Given that one of the stated aims of OIRA review is to align agency rulemaking with presidential priorities, the Independent Agency Regulatory Analysis Act would lead to more presidential influence over the FCC and other independent agencies rather than less. Taking the Committee majority's concerns about the independence of the FCC at face value, we encourage Senators on the committee to revisit and withdraw their support for the Independent Agency Regulatory Analysis Act.

### C. The Clean Water Rule

Issued by the Environmental Protection Agency and Army Corps of Engineers, the Clean Water Rule: Definition of "Waters of the United States" was published in the Federal Register on June 29, 2015 and became effective on August 28, 2015. The purpose of the rule is to provide

<sup>61</sup> David Burnham, "Reagan Role in FCC Case Assailed," New York Times, February 4, 1984, available at: <http://www.nytimes.com/1984/02/04/arts/reagan-role-in-fcc-case-assailed.html> (noting the interests of Reagan's personal friends in the outcome of the regulatory dispute).

<sup>62</sup> John Lippman, "Sununu Defends White House Stand on TV Rerun Rules," Los Angeles Times, February 16, 1991, available at: [http://articles.latimes.com/1991-02-16/business/ft-984\\_1\\_white-house](http://articles.latimes.com/1991-02-16/business/ft-984_1_white-house).

<sup>63</sup> John Broder, "Clinton to Ask F.C.C. to Consider Restricting Liquor Commercials," New York Times, April 1, 1997, available at: <http://www.nytimes.com/1997/04/01/us/clinton-to-ask-fcc-to-consider-restricting-liquor-commercials.html>.

<sup>64</sup> David Ho, "Bush Administration Pushes FCC on Media Ownership Review," Government Technology, April 25, 2003, available at: <http://www.govtech.com/policy-management/Bush-Administration-Pushes-FCC-on-Media.html>.

<sup>65</sup> Tom Wheeler, "This Is How We Will Ensure Network Neutrality," Wired, February 4, 2015, available at: <http://www.wired.com/2015/02/fcc-chairman-wheeler-net-neutrality>.

definitional clarity as to the waters regulated under the Clean Water Act, and to further the Act's purpose to restore and maintain the chemical, physical and biological integrity of the Nation's waters. Although the Clean Water Rule has become the source of contentious debate, it is in fact a modest measure aiming to provide more administrative certainty, and it actually reduces the regulatory scope of navigable waters and their tributaries (the key terms that determine the geographic application of the Clean Water Act). Nonetheless, in providing more regulatory certainty, the Clean Water Rule should contribute to the effective enforcement of the Clean Water Act, leaving our nation with cleaner and healthier streams and rivers.

There is little doubt that the Clean Water Rule is needed. The precise scope of Clean Water Act jurisdiction became unclear following U.S. Supreme Court decisions in *Solid Waste Agency of Northern Cook County (SWANCC) v. U.S. Army Corps of Engineers*, 531 U.S. 159 (2001) and *Rapanos v. United States* 126 S.Ct. 2208 (2006). In his concurring opinion in *Rapanos*, Chief Justice Roberts harshly criticized the agencies for not issuing a definitional rule: "Given the broad, somewhat ambiguous, but nonetheless clearly limiting terms Congress employed in the Clean Water Act, the Corps and the EPA would have enjoyed plenty of room to operate in developing some notion of an outer bound to the reach of their authority."<sup>66</sup>

Following the instructions of Chief Justice Roberts and others, the Clean Water Rule establishes a more precise definition of navigable waters and tributaries.<sup>67</sup> A covered tributary must show the physical features of flowing water – a bed, bank and ordinary high water mark. The rule covers certain waters adjacent to rivers, lakes and their tributaries, because science shows these waters can impact downstream waters. The rule does not cover ditches not constructed in streams and that flow only when it rains.<sup>68</sup> The rule explicitly does not include puddles.<sup>69</sup> It does not change how storm sewer systems are treated under the Clean Water Act. Importantly to advance the objective of predictability and certainty, the rule limits the use of case-specific determinations.

The scope of the rule is narrower than previously existing regulation,<sup>70</sup> although it will encompass some waters that had not been covered under field practice following the Supreme Court's decisions in *SWANCC* and *Rapanos*.

Although the Clean Water Rule is merely definitional, and even though the scope of covered waters will be less than historic practice, this rule is vitally important. It will advance predictability and certainty in application of the Clean Water Rule, and should thereby help

<sup>66</sup> *Rapanos v. United States, Roberts, C.J. Concurring*, 126 S.Ct. 2208, 2236 (2006).

<sup>67</sup> Final Rule Text, § 328.3 See also: [https://www.epa.gov/sites/production/files/2015-05/documents/fact\\_sheet\\_summary\\_final\\_1.pdf](https://www.epa.gov/sites/production/files/2015-05/documents/fact_sheet_summary_final_1.pdf).

<sup>68</sup> Final Rule Text, § 230.3(s)(2)(iii)

<sup>69</sup> Final Rule Text, § 230.3(s)(2)(iv)(G)

<sup>70</sup> Federal Register, Vol. 80, No. 124, 37054 ("The scope of jurisdiction in this rule is narrower than that under the existing regulation. Fewer waters will be defined as "waters of the United States" under the rule than under the existing regulations, in part because the rule puts important qualifiers on some existing categories such as tributaries. In addition, the rule provides greater clarity regarding which waters are subject to CWA jurisdiction, reducing the instances in which permitting authorities, including the states and tribes with authorized section 402 and 404 CWA permitting programs, would need to make jurisdictional determinations on a case-specific basis.")

enhance the cleanliness and health of our nation's waters. It is hard to exaggerate the importance of this objective. Almost one in three Americans – roughly 117 million people – get their drinking water from streams that lacked clear protection before issuance of the Clean Water Rule.<sup>71</sup> Tens of millions of Americans every year use the waters for fishing, paddling, swimming and other forms of recreation. And countless businesses – from recreation industries to agriculture, tourism to manufacturing – rely on clean water.

A decade in the making, the Clean Water Rule was subjected to an incredibly rigorous process of expert review and public comment. Vermont Law School Professor Patrick Parenteau, a Clean Water Act expert, comments, “In my 40+ years of experience with the Clean Water Act I cannot recall any other rulemaking that received more scientific review, public scrutiny, critical analysis, open debate and responsive action by the agencies” than the Clean Water Rule.<sup>72</sup>

Here's why Parenteau reaches that conclusion:

- In advance of the rulemaking, the EPA and Army Corps held more than 400 public meetings around the country, making special efforts to hear from farmers across the nation.
- EPA and the Corps met with hundreds of local officials, with EPA's Local Government Advisory Committee hosting a series of meetings around the country.
- The EPA's Science Advisory Board convened a special expert panel to review the EPA's draft report on the connectivity or isolation of streams and wetlands from larger bodies of water, such as rivers and lakes. This concerned arguably the central issue in the Clean Water Rule; tributaries and smaller bodies of water that have downstream impacts would be covered. The panel found that “the review and synthesis of the literature describing connectivity of streams to downstream waters reflects the pertinent literature and is well grounded in current science,” but argued as well that the agency had taken too conservative an approach in identifying connectivity.<sup>73</sup>
- The EPA and Army Corps prepared an extremely detailed, 75-page economic analysis of the costs and benefits of the proposed rule. The analysis noted that because the Clean Water Rule imposes no new regulatory requirements and, separately, because it will actually reduce the scope of waters covered as compared to the historic regulatory interpretation, it can be argued that the new rule will impose no new costs whatsoever. But the analysis also recognized that there will be expanded jurisdiction as compared to recent practice, and analyzed the impact in extraordinary detail. In sum, the analysis

<sup>71</sup> <https://www.epa.gov/cwa-404/geographic-information-systems-analysis-surface-drinking-water-provided-intermittent>

<sup>72</sup> Patrick Parenteau, testimony before the Senate Judiciary Committee, June 10, 2015, available at: <<https://www.judiciary.senate.gov/imo/media/doc/06-10-15%20Parenteau%20Testimony.pdf>>.

<sup>73</sup> Letter from David T. Allen and Amanda D. Rodewald to EPA Administrator Gina McCarthy, October 17, 2014, available at: [https://yosemite.epa.gov/sab/sabproduct.nsf/02ad90b136fc21ef85256eba00436459/AF1A28537854F8AB85257D74005003D2/\\$File/EPA-SAB-15-001+unsigned.pdf](https://yosemite.epa.gov/sab/sabproduct.nsf/02ad90b136fc21ef85256eba00436459/AF1A28537854F8AB85257D74005003D2/$File/EPA-SAB-15-001+unsigned.pdf).

concluded that economic benefits will definitely outpace costs, by as much as two-to-one, depending on what assumptions are made.<sup>74</sup>

- The rule underwent notice-and-comment, per the Administrative Procedure Act. But the notice-and-comment process was not standard. The deadline for submitting comments was extended twice beyond the original 60-day comment period. The agencies received more than 1 million comments (the vast majority form comments, in support of the rule). The agencies meticulously organized and responded to each comment. In addition to broad responses to the mass mailing campaigns, the agencies grouped comments into 17 distinct topic areas, and replied to every substantive issue and concern raised. Meaningful changes were made to the final rule in light of comments received. Altogether, those materials total more than a staggering 7,300 pages.<sup>75</sup>

Surprisingly, the EPA has actually been attacked for its effort at transparency and public engagement. The agency utilized a variety of online and social media tools to publicize its activities around the Clean Water Rule and urge public participation in the rulemaking process. Tenuous arguments have been made that a disclosure of EPA involvement was missing from tweets that were sent as part of a Thunderclap (although the agency was prominently labeled on the Thunderclap itself), and that the agency linked to two web pages that urged citizens to contact their Members of Congress.<sup>76</sup> Whatever the merits of these questionable claims, they should not obscure that they are made in the context of agency proactive efforts at openness and public involvement. Nor should it be lost that they concern very minor matters as compared to the extraordinarily robust and open process that the agencies conducted to develop the final rule.

### III. Improving Regulation

Recognizing the crucial role that regulation plays in improving our standard of living underscores the importance of ensuring that the regulatory process works well. Regulators should be nimble and flexible, able to act quickly with appropriate new rules in response to changing technologies, new science and social learning, evolutions in industry structure and other emerging trends and developments. At the same time, regulators must effectively enforce new and old rules; they must be adequately funded, equipped with needed regulatory tools including inspection powers and sufficiently tough penalties for lawbreakers, independent from the parties they regulate while maintaining appropriate responsiveness, and guided by leadership with sufficient political will and protected from interference. Unfortunately, those qualities by and large do not describe the current state of the regulatory process or enforcement.

There is an acute need for regulatory reform, to address pervasive and harmful delay in the rulemaking process, increase and improve regulatory enforcement, improve transparency,

<sup>74</sup> Environmental Protection Agency and U.S. Department of the Army, Economic Analysis of the EPA-Army Clean Water Rule, May 20, 2015, available at: [https://www.epa.gov/sites/production/files/2015-06/documents/508-final\\_clean\\_water\\_rule\\_economic\\_analysis\\_5-20-15.pdf](https://www.epa.gov/sites/production/files/2015-06/documents/508-final_clean_water_rule_economic_analysis_5-20-15.pdf).

<sup>75</sup> Response to comments for the Clean Water Rule: Definition of “Waters of the United States,” available at: <https://www.epa.gov/cleanwaterrule/response-comments-clean-water-rule-definition-waters-united-states>.

<sup>76</sup> Letter from Susan Poling, GAO General Counsel, to Senator James Inhofe, December 14, 2015, available at: [http://www.epw.senate.gov/public/\\_cache/files/b7bb198f-bbd4-4011-a756-b3627ecacfa1/gao-opinion-epa-social-media-121415.pdf](http://www.epw.senate.gov/public/_cache/files/b7bb198f-bbd4-4011-a756-b3627ecacfa1/gao-opinion-epa-social-media-121415.pdf).

address undue industry influence over the rulemaking process, address uneven judicial review of regulations, and adopt pro-competitive rules to level the playing field for small business and improve the economy and consumer well-being. I discuss these problem areas in this portion of my testimony, concluding each section or subsection with proposed remedies.

#### **A. Combating unreasonable delay**

Unreasonable delay permeates almost all aspects of the rulemaking process. The consequences of delay are serious. As opposed to issuance of new rules, delay creates the regulatory uncertainty that many business spokespeople denounce. Delay also means that lives are needlessly lost, injuries needlessly suffered, environmental harm needlessly permitted, consumer rip-offs extended, and more.

Four years ago, Public Citizen conducted an analysis of public health and safety rulemakings with congressionally mandated deadlines.<sup>77</sup> Our analysis showed that most rules are issued long after their deadlines have passed, needlessly putting American lives at risk. Of the 159 rules analyzed, 78 percent missed their deadline. Federal agencies miss these deadlines for a variety of reasons, including having to conduct onerous analyses, dealing with politically motivated delays, inadequate resources or agency commitment, and fear of judicial review.

A high proportion of pending rules with statutory deadlines are mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The financial regulatory agencies remain far behind schedule. The most recent report from the law firm DavisPolk finds that, through the last quarter of 2015, regulators have still not complied with a quarter of the 271 statutory deadlines that have passed. This is five-and-a-half years after passage of the Act.<sup>78</sup>

The problem of protracted delay is pervasive in the rulemaking sphere and reflective of a rulemaking process gone askew. This is far more than a “bureaucratic” problem; the source of the problem is not inept government officials and workers, but a thicket of legislatively mandated process and multiple analyses, along with inappropriate influence exerted by and for regulated parties. And the consequences are far more severe than a generic inefficiency—lengthy delay costs money and lives; it permits ongoing ecological destruction and the infliction of needless injury; it enables fraudsters and wrongdoers to perpetuate their misdeeds; and it denies businesses the regulatory certainty they need to make sound investment decisions.

Although extended delay is arguably the defining feature of rulemaking, the extent, severity, causes and consequences of such delay are not well understood. I highlight several illustrative examples here to illuminate these matters.

#### **1. Oil Train Safety**

<sup>77</sup> Mouzoon, N. (2012). *Public Safeguards Past Due: Missed Deadlines Leave Public Unprotected*. Public Citizen. Available from: <<http://www.citizen.org/documents/public-safeguards-past-due-report.pdf>>.

<sup>78</sup> DavisPolk. (2016) *Dodd-Frank Progress Report*. Available from: <<http://www.davispolk.com/Dodd-Frank-Rulemaking-Progress-Report>>.

Last year, the U.S. Department of Transportation finalized new standards for trains transporting highly volatile oil, often through highly populated areas. The rule was a long-overdue response to the sharp increase in domestic oil production and rail shipment of oil and ethanol and a resulting series of deadly oil train disasters. In strengthening standards for oil tank car safety, requiring new braking standards, and designating new procedures for oil trains including notification to local government agencies, the rule should reduce the incidence oil train derailments and explosions.<sup>79</sup>

The final issuance of the rule followed justifiable bipartisan criticism that the Department of Transportation had taken too long to put new rules in place while multiple oil train derailments and explosions occurred across the country. These explosions and crashes have led to numerous deaths, and shaken up communities across the country. Elected officials rightly demanded action, and were furious about the delays in responsive rulemaking. Safety experts echoed the concern. “Federal requirements simply have not kept pace with evolving demands placed on the railroad industry and evolving technology and knowledge about hazardous materials and accidents,” testified the chair of the National Transportation Safety Board.<sup>80</sup>

The Department itself shared frustration with the slow pace of its rulemaking. One of the regulators made clear why the Department was unable to move faster saying, “To be clear, I think we have to function in the regulatory process that exists. And it's not built for speed. I wish it was. And no one is more frustrated by our regulatory process and how long it takes than I am on occasion. But if we are trying to govern and regulate as quickly as we possibly can, the rulemaking process is not the way to do it.”<sup>81</sup>

The Department could have expedited issuance of the rules by foregoing optional rulemaking steps that added to the regulatory delay. The Department’s decision to issue an advanced notice of proposed rulemaking (ANPRM) instead of directly proceeding to propose a draft rule, likely added a year or more to the oil train rulemaking process.

Unfortunately, this committee has passed legislation that would mandate the extra procedural step of ANPRMs for all major rules such as the oil train rule.<sup>82</sup> The oil train rule delay makes clear that there are real-world consequences – often a matter of life and death – to measures that delay the rulemaking process. It is a reminder as well that policymakers who support measures to slow and complicate the rulemaking process may find that, if they succeed, the required delays will boomerang to block regulatory action in areas of their priority concern.

## 2. Cranes and derricks.

<sup>79</sup> <https://www.transportation.gov/briefing-room/final-rule-on-safe-rail-transport-of-flammable-liquids>

<sup>80</sup> Chris A. Hart, testimony before the Committee on Transportation and Infrastructure, U.S. House of Representatives, “Oversight of the Ongoing Rail, Pipeline, and Hazmat Rulemakings,” April 14, 2015, available at: <http://transportation.house.gov/uploadedfiles/2015-04-14-hart.pdf>.

<sup>81</sup> Sarah Feinberg, Acting Administrator, Federal Railroad Administration, U.S. House Transportation and Infrastructure Committee, Oversight of the Ongoing Rail, Pipeline, and Hazmat Rulemakings, April 14, 2015, available at: <http://transportation.house.gov/calendar/eventsingle.aspx?EventID=398734>.

<sup>82</sup> See e.g. S. 1820, Early Participation In Regulations Act of 2015 (114<sup>th</sup> Congress) available at <https://www.congress.gov/bills/114/congress/senate-bill/1820>.



The Occupational Safety and Health Administration's cranes and derricks rule, adopted in 2010, is designed to improve construction safety. By the late 1990s, construction accidents involving cranes were killing 80 to 100 workers a year. OSHA later estimated that a modernized rule would prevent about 20 to 40 of those annual tragedies. Worker safety advocates and the construction industry alike wanted an updated rule.

Nonetheless, it took a dozen years to get a final rule adopted. "During the dozen years it took to finalize the cranes rule," a Public Citizen report summarized, "OSHA and other federal agencies held at least 18 meetings about it. At least 40 notices were published in the Federal Register. OSHA was required by a hodgepodge of federal laws, regulations and executive orders to produce several comprehensive reports, and revisions to such reports, on matters such as the makeup of industries affected by the rule, the number of businesses affected, and the costs and benefits of the rule. OSHA also was repeatedly required to prove that the rule was needed, that no alternative could work, and that it had done everything it could to minimize the effects on small businesses. The regulatory process afforded businesses at least six opportunities to weigh in with concerns that the agency was required to address."<sup>83</sup>

### 3. Silica rule.

After more than a dozen years of delay, OSHA's life-saving silica dust standard is finally set to take effect this year. More than two million workers in the United States are exposed to silica dust, especially construction workers and others who operate jackhammers, cut bricks or use sandblasters. Inhaling the dust causes a variety of harmful effects, including lung cancer, tuberculosis, and silicosis (a potentially fatal respiratory disease). The rule will reduce the permissible exposure limit for silica to 50 micrograms per cubic meter (from the currently allowed 100) over an 8-hour workday. "OSHA estimates that the proposed rule would prevent between 579 and 796 fatalities annually—375 from non-malignant respiratory disease, 151 from end-stage renal disease, and between 53 and 271 from lung cancer—and an additional 1,585 cases of moderate-to-severe silicosis annually."<sup>84</sup>

The new standard requires employers to measure exposures, conduct medical exams for workers with high exposures and train workers about the hazards of silica. It requires effective measures to reduce silica exposure, which "can generally be accomplished by using common dust control methods, such as wetting down work operations to keep silica-containing dust from getting into the air, enclosing an operation ('process isolation'), or using a vacuum to collect dust at the point where it is created before workers can inhale it,"<sup>85</sup> while giving businesses flexibility in choosing appropriate control methods.

<sup>83</sup> Lincoln, T. and Mouzoon, N. (2011, April.) *Cranes & Derricks: The Prolonged Creation of a Key Public Safety Rule*. Public Citizen. p. 4. Available from: <<http://www.citizen.org/documents/CranesAndDerricks.pdf>>.

<sup>84</sup> OSHA. (2013). *Preliminary Economic Analysis and Initial Regulatory Flexibility Analysis: Supporting document for the Notice of Proposed Rulemaking for Occupational Exposure to Crystalline Silica*. Available at: [https://www.osha.gov/silica/Silica\\_PEA.pdf](https://www.osha.gov/silica/Silica_PEA.pdf).

<sup>85</sup> OSHA, OSHA's Proposed Crystalline Silica Rule: Overview, available at: [https://www.osha.gov/silica/factsheets/OSHA\\_FS-3683\\_Silica\\_Overview.html](https://www.osha.gov/silica/factsheets/OSHA_FS-3683_Silica_Overview.html).

OSHA has long acknowledged that its current silica dust standard, adopted in 1971, is obsolete.<sup>86</sup> The first concrete action it took to update the standard was in October 2003, when it convened a small business panel to review its proposed rule. In 2011, OSHA submitted to OIRA a draft proposed rule to reduce exposure to deadly silica dust. Although OIRA is supposed to complete reviews in three months, it took years for OIRA to complete the review. No explanation for this delay ever emerged. After OIRA finally released the rule, the rule remained stuck at OSHA.

Dating to OSHA's 1998 move of silica exposure standards to the pre-rule stage, the inexcusable delay in finalizing an updated health standard translates into the needless deaths of roughly 12,000 people. Inexcusable is really far too gentle a term; the industry-led obstruction of the rule cost thousands of lives – not statistical abstractions, but the lives of real workers.

Silica-related disease is not evenly distributed across the U.S. population. As a result, the benefits of the new rule will be felt most strongly among working class communities and communities of color. In Michigan, studies show the incidence of silicosis in African Americans is almost 6 times greater than that of Caucasians.<sup>87</sup> Latino workers now constitute 24 percent of the workforce in foundries, and almost 26 percent of the workforce in construction, are especially at risk for working jobs where silica dust exposure is paired with a lack of protection.

OSHA estimates the rule will provide average net benefits of about \$2.8 to \$4.7 billion annually over the next 60 years (benefits calculated by assigning a dollar value to each anticipated life saved and illness avoided).

#### 4. Truck driver training.

In 1991, Congress passed a law requiring a rulemaking on training for entry-level commercial motor vehicle operators. More than 20 years, three lawsuits, and another statutory mandate later, the Department of Transportation still has not enacted regulations requiring entry-level drivers to receive training in how to drive a commercial motor vehicle. It now says it plans to complete the rule this year.<sup>88</sup>

In the Intermodal Surface Transportation Efficiency Act (ISTEA) of 1991, Congress required the Secretary of Transportation to report to Congress on the effectiveness of private sector training of entry-level commercial motor vehicle drivers by December 18, 1992, and to complete a rulemaking proceeding on the need to require training of all entry level drivers of commercial motor vehicles by December 18, 1993. The required report, which was submitted to Congress on February 2, 1996 (slightly more than three years later), concluded that training of new commercial motor vehicle drivers was inadequate; in an accompanying analysis, the agency determined that the benefits of an entry-level driver training program would outweigh its costs. It

<sup>86</sup> OSHA *Occupational Exposure to Crystalline Silica*, 75 Fed. Reg. 79,603 (2010, Dec. 20).

<sup>87</sup> Rosenman, K. and Reilly, M.J. (2014, July 1). 2012 *Annual Report Tracking Silicosis and Other Work-Related Lung Diseases in Michigan*, Michigan State University, available at: [http://www.oem.msu.edu/userfiles/file/Annual%20Reports/Silica/2012Silicosis\\_OccLungDiseaseAnnRpt.pdf](http://www.oem.msu.edu/userfiles/file/Annual%20Reports/Silica/2012Silicosis_OccLungDiseaseAnnRpt.pdf).

<sup>88</sup> A full account of this history is included in In Re Advocates for Highway and Auto Safety: Petition for Writ of Mandamus, September 18, 2014. Available from: <http://www.citizen.org/documents/in-re-advocates-for-highway-and-auto-safety-petition-for-writ-of-mandamus.pdf>.

requested comments on the studies and held one public hearing on training entry-level drivers. In the next six years, however, the agency took no steps towards issuing a rule on entry-level driver training.

In November 2002, organizations concerned about motor vehicle safety filed a petition for a writ of mandamus in the DC Circuit Court of Appeals, seeking an order directing the Secretary of Transportation to fulfill his statutory duty to promulgate overdue regulations relating to motor vehicle safety, including the regulation on entry-level driver training. As part of a settlement agreement between the organizations and DOT, DOT agreed to issue a final rule on minimum training standards for entry-level commercial motor vehicle drivers by May 31, 2004.

On August 15, 2003, almost 12 years after ISTEA was enacted, DOT (through the Federal Motor Carrier Safety Administration, FMCSA) published a notice of proposed rulemaking on minimum training requirements for entry-level commercial motor vehicle operators, and on May 21, 2004, it published a final rule.

Although the agency expressly acknowledged that training for entry-level drivers was inadequate and stated its belief that a 360-hour model curriculum developed by the Federal Highway Administration that includes extensive behind-the-wheel training “represents the basis for training adequacy,” it proposed instead a weak rule that required only 10 hours of training.

Advocates for Highway and Auto Safety, among others, subsequently filed a petition for review of the final rule, arguing that the rule was arbitrary and capricious because it did not require entry-level drivers to receive any training in how to operate a commercial motor vehicle. The DC Circuit agreed, holding that the FMCSA had “adopted a final rule whose terms have almost nothing to do with an ‘adequate’ CMV [commercial motor vehicle] training program.”

On December 26, 2007, approximately two years after the court ruling, FMCSA issued a stronger proposed rule. But, four years after the comment period had closed, the agency still had not issued a final rule.

In 2012, Congress again directed DOT to conduct a rulemaking on the issue, requiring a final rule by October 1, 2013.

Yet instead of moving forward, the FMSCA published notice in September 2013 that it was withdrawing its proposed rule.

We still have no proposed rule. In September 2014, Public Citizen with Advocates for Highway Safety filed another lawsuit, on behalf of a number of parties, asking that the agency be ordered to issue a rule in compliance with the law. That case is now stayed, in reliance on an agency statement that it plans to issue a rule by September 2016.

More than 20 years have passed since Congress ordered the DOT to adopt an appropriate truck driver training rule, and there is still no rule. This is due in large part to the agency’s overly cozy relationship with the trucking industry. Congress has mandated a driver training rule—twice—out of the recognition that better driver training will save lives; and the two-decade-long refusal

of the agency to comply with Congressionally imposed obligations means lives have been—and continue to be—lost needlessly.

### 5. Backover rule<sup>89</sup>

One night in 2002, Dr. Greg Gulbransen was backing up his SUV in his driveway when his two-year-old son Cameron darted out into the driveway behind the vehicle. Too small to be seen by his father using any of the vehicle's rearview or sideview mirrors, Cameron was struck by the moving car and killed. Dr. Gulbransen's tragedy is not an isolated case; each week, 50 children are injured, two fatally, in these "backover" crashes, that is, collisions in which a vehicle moving backwards strikes a person (or object) behind the vehicle. Each year on average, according to the Department of Transportation, backovers kill 292 people and injure 18,000 more—most of whom are children under the age of five, senior citizens over the age of 75, or persons with disabilities. Backovers generally occur when the victim is too small to be seen in the rearview mirror of the vehicle or too slow to move out of the way of the vehicle, even one moving at slow speed.

To prevent the injuries and deaths caused by backovers, in 2008 Congress passed and the President signed the Cameron Gulbransen Kids Transportation Safety Act. The Gulbransen Act directed DOT to revise an existing federal motor vehicle safety standard to expand the area that drivers must be able to see behind their vehicles. (This can be done through the use of rear-view cameras, or other technologies.) The Gulbransen Act mandated that DOT issue the final rule within three years of the law's enactment—by February 28, 2011. The Act also allowed DOT to establish a new deadline for the rulemaking, but only if the otherwise-applicable deadline "cannot be met."

When it prepared a draft final rule in 2010, DOT estimated that the proposed rule, which specified an area immediately behind each light vehicle that a driver must be able to see when the car is in reverse gear, would prevent between 95 and 112 deaths and between 7,072 and 8,374 injuries each year.

DOT failed to meet the February 2011 deadline. Instead, DOT repeatedly set a new "deadline," failed to meet it, and then set yet another "deadline," although the agency never made a showing that the statutory deadline could not be met.

In light of the extent of the delay, the repeated self-granted extensions, and the hundreds of preventable deaths and thousands of preventable injuries that will occur while the public waits for the final rule, Public Citizen filed a petition with the United States Court of Appeals for the Second Circuit seeking a writ of mandamus compelling DOT to issue the rule within 90 days. The petition was filed September 25, 2013 on behalf of Dr. Gulbransen, Sue Auriemma (another parent who backed into her own child), and the consumer safety groups Advocates for Highway and Auto Safety, KidsAndCars.org, and Consumers Union. On March 31, 2014, one day before

<sup>89</sup> A full account of this history is available from *In Re Dr. Greg Gulbransen: Petition for a Writ of Mandamus*, September 25, 2013. Available from: <<http://www.citizen.org/documents/In-re-Gulbransen-Backover-Petition.pdf>>.

the Second Circuit was scheduled to hear argument in the case, DOT issued the rear visibility safety standard that petitioners sought.

In this case, much remains unknown about the cause of the protracted delay. The department had been on track to issue a rule by or near the Congressional deadline, but then pulled back. It is widely believed that the rule was delayed by OIRA out of concern about the agency's cost-benefit analysis—the auto makers predictably made unrealistic claims about potential cost—or by political intervention from high officials in the White House.

Whatever the cause, that delay led to the pointless deaths of hundreds and tens of thousands of injuries. What a horrible tragedy it is for a parent to live with the knowledge that he or she ran over their child. But what a monstrous outrage for those tragedies to perpetuate because corrective action was delayed due to inappropriate political influence.

#### **6. Executive pay ratio rule.**

Section 953(b) of the Dodd Frank Act requires companies to disclose the ratio of CEO-to-median workers' pay. This is perhaps the simplest of Dodd Frank required rules. Companies already disclose their CEO compensation. Basic accounting requires them to know what they pay their employees, and determining the median pay for all employees is a simple enough determination. Figuring out the ratio between the two is a simple enough arithmetic calculation. Somehow, however, the nation's biggest firms have proffered the view that such a disclosure requirement and calculation would be incredibly burdensome. This hard-to-swallow claim, apparently, paralyzed the Securities and Exchange Commission. It proposed a rule in September 2013 with a standard 60-day comment period; but the final rule was not issued until August 2015. This is a modest measure to be sure—though it will provide important information to both investors and employees—but precisely because of its simplicity, the SEC should have been able to issue a rule expeditiously.<sup>90</sup>

#### **7. Blowout Preventers**

The April 20, 2010 explosion aboard the Deepwater Horizon in BP's Macondo Prospect killed 11 people and ultimately spewed 5 million barrels of oil directly into the Gulf of Mexico until the Coast Guard finally certified that efforts to permanently plug the well succeeded after 5 months.

The disaster was the result of cascading failures by all parties involved: BP, the manager of the operation; Transocean, the owner of the semi-submersible oil exploration platform; Halliburton, the company in charge of the oil well cementing; and Cameron International Corp., the Houston supplier of the failed blowout preventer. Cameron ended up agreeing to pay BP \$250 million in December 2011 to settle the company's legal liabilities associated with the failures of its blowout preventer.<sup>91</sup>

<sup>90</sup> See Naylor, B. (2015, June 2.) Mary Jo Wait. Huffington Post. Available from: <[http://www.huffingtonpost.com/bartlett-naylor/mary-jo-wait\\_b\\_7494336.html](http://www.huffingtonpost.com/bartlett-naylor/mary-jo-wait_b_7494336.html)>.

<sup>91</sup> Tom Fowler, "Cameron Will Pay BP to Settle Spill Claims," Wall Street Journal, December 17, 2011, available at: [www.wsj.com/articles/SB10001424052970204466004577102050498485784](http://www.wsj.com/articles/SB10001424052970204466004577102050498485784).

Cameron's blowout preventer was a five-story, 400-ton device that sat on the ocean floor, connected to the wellhead, that was supposed to "contain pressure within the wellbore and halt an uncontrolled flow of hydrocarbons to the rig,"<sup>92</sup> known as a blowout. A blowout preventer features a number of different components to allow deep water drillers to maintain well control, including the device's last line of defense, a blind shear ram, that cuts the drill pipe to seal the well in the event of a blowout. But all of Cameron's blowout preventer features failed on April 20 and in the days afterward.

Subsequent independent investigations detailed the failures of blowout preventers to be properly designed and tested to successfully prevent blowouts in deep sea drilling operations.

President Obama created the National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling one month after the explosion.<sup>93</sup> The Commission's final report, issued in January 2011, faulted the industry's reliance on self-testing by blowout preventer manufacturers and well operators, and the fact that these tests were done on land, rather than under pressure deep underwater. In addition, the Commission recommended "design modifications" in blowout preventers to ensure they are "equipped with sensors or other tools to obtain accurate diagnostic information."<sup>94</sup>

This self-certification that failed to replicate actual operating conditions was one reason that the U.S. Department of Interior proposed new rules governing just the testing blowout preventers on September 30, 2010,<sup>95</sup> including a new requirement for "independent third party verification that the blind-shear rams are capable of cutting any drill pipe in the hole under maximum anticipated surface pressure," minimum personnel training requirements for blowout preventer operators, and additional required testing once the blowout preventer is installed on the seafloor.<sup>96</sup> While first proposed in September 2010, the rule for third-party, independent, real-condition testing of blowout preventers did not become final until August 2012.<sup>97</sup>

<sup>92</sup> National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, Final Report, January 11, 2011, p. 114, available at: <http://cybercemetery.unt.edu/archive/oilspill/20121211005636/http://www.oilspillcommission.gov/sites/default/files/documents/FinalReportPartII.pdf>.

<sup>93</sup> [www.whitehouse.gov/the-press-office/2010/06/01/execution-order-national-commission-bp-deepwater-horizon-oil-spill-and-offshore-dri](http://www.whitehouse.gov/the-press-office/2010/06/01/execution-order-national-commission-bp-deepwater-horizon-oil-spill-and-offshore-dri)

<sup>94</sup> National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, Final Report, January 11, 2011, p. 35, available at: <http://cybercemetery.unt.edu/archive/oilspill/20121211005636/http://www.oilspillcommission.gov/sites/default/files/documents/FinalReportPartII.pdf>.

<sup>95</sup> [www.doi.gov/news/pressreleases/Salazar-Announces-Regulations-to-Strengthen-Drilling-Safety-Reduce-Risk-of-Human-Error-on-Offshore-Oil-and-Gas-Operations](http://www.doi.gov/news/pressreleases/Salazar-Announces-Regulations-to-Strengthen-Drilling-Safety-Reduce-Risk-of-Human-Error-on-Offshore-Oil-and-Gas-Operations).

<sup>96</sup> [www.doi.gov/sites/doi.gov/files/migrated/news/pressreleases/upload/093010\\_Fact-Sheet\\_Drilling-Safety-Rule.pdf](http://www.doi.gov/sites/doi.gov/files/migrated/news/pressreleases/upload/093010_Fact-Sheet_Drilling-Safety-Rule.pdf).

<sup>97</sup> Final Rule, available at: [www.bsee.gov/uploadedFiles/BSEE/Regulations\\_and\\_Guidance/Recently\\_Finalized\\_Rules/Final\\_Drilling\\_Safety\\_Rule/AA02%20FR%20publication%20\(08-22-12\)%20\(1\).pdf](http://www.bsee.gov/uploadedFiles/BSEE/Regulations_and_Guidance/Recently_Finalized_Rules/Final_Drilling_Safety_Rule/AA02%20FR%20publication%20(08-22-12)%20(1).pdf).

While third-party, independent, real-condition testing is important, investigations concluded that a bigger challenge was that blowout preventers needed to be redesigned to actually work effectively.

A December 2011 report by the National Academy of Engineering concluded that blowout preventer systems “are neither designed nor tested to operate in the dynamic conditions that occurred during the accident” and should be “redesigned, rigorously tested, and maintained to operate reliably.”<sup>98</sup>

Similarly, on April 12, 2016, the U.S. Chemical Safety and Hazard Investigation Board released a draft report on the Deepwater Horizon disaster, with one of their primary conclusions: “Testing limitations masked latent failures of the Deepwater Horizon BOP, affecting its operation on the day of the incident, *and these latent failures will continue to exist for similarly designed blowout preventers unless modifications are made to current standard industry testing protocols*”<sup>99</sup> (emphasis added).

The origins of the latest blowout preventer rule, designed to overhaul the design of blowout preventers, began with a technical conference hosted by the Bureau of Safety and Environmental Enforcement in May 2012,<sup>100</sup> with then-Deputy Interior Secretary David Hayes claiming a proposed rule would come by September 2012.<sup>101</sup>

But the Bureau of Safety and Environmental Enforcement didn’t send its proposed rule to the Office of Information and Regulatory Affairs until December 11, 2014.<sup>102</sup> The proposed rule wasn’t published in the Federal Register until April 2015.<sup>103</sup> The final rule wasn’t released until April, 2016.

It is unfathomable that the primary regulatory response to the worst environmental disaster in U.S. history took six years. Indeed, “unfathomable” was the very term used to describe the delay by S. Elizabeth Birnbaum, the head of the Minerals Management Service at the time of the BP oil blowout – a full two years before the final rule was issued!

It’s unfathomable that the administration has failed to act on the findings of the December 2011 report of the National Academy of Engineering, which gave us some very bad news about Deepwater Horizon’s blowout preventer.

<sup>98</sup> National Academy of Engineering, Macondo Well-Deepwater Horizon Blowout, December 14, 2011, available at: [www.nae.edu/Publications/Reports/53926.aspx](http://www.nae.edu/Publications/Reports/53926.aspx).

<sup>99</sup> U.S. Chemical Safety and Hazard Investigation Board, “Drilling Rig Explosion and Fire at the Macondo Well,” April 20, 2010, p. 8, available at: [www.dropbox.com/s/oadxmn7me0xbdg9/20160412%20Macondo%20Full%20Exec%20Summary.pdf](http://www.dropbox.com/s/oadxmn7me0xbdg9/20160412%20Macondo%20Full%20Exec%20Summary.pdf).

<sup>100</sup> [www.bsee.gov/BSEE-Newsroom/Press-Releases/2012/Secretary-Salazar,-BSEE-Director-Watson-to-Kick-Off-Technical-Forum-on-Next-Generation-Blowout-Preventer-and-Control-Systems/](http://www.bsee.gov/BSEE-Newsroom/Press-Releases/2012/Secretary-Salazar,-BSEE-Director-Watson-to-Kick-Off-Technical-Forum-on-Next-Generation-Blowout-Preventer-and-Control-Systems/)

<sup>101</sup> Paul Voosen, “Regs for blowout preventers imminent,” Greenwire, May 22, 2012.

<sup>102</sup> Phil Taylor, “White House reviewing rule to reduce blowout threats,” E&E Reporter, December 15, 2014.

<sup>103</sup> Final Rule, [www.bsee.gov/uploadedFiles/BSEE/Regulations\\_and\\_Guidance/Recently\\_Finalized\\_Rules/Well\\_Control\\_Rule/2015-08587.pdf](http://www.bsee.gov/uploadedFiles/BSEE/Regulations_and_Guidance/Recently_Finalized_Rules/Well_Control_Rule/2015-08587.pdf).

Its massive cutting blades were supposed to slice through the drill pipe to stop the flow of gushing oil. But it turned out that these huge pieces of equipment were not adequately engineered to stop emergency blowouts in deep water.

The academy's report was detailed and damning. Deepwater Horizon's blowout preventer "was neither designed nor tested for the dynamic conditions that most likely existed at the time that attempts were made to recapture well control," the report said. More troubling, the shortcomings of Deepwater's equipment "may be present" at other deepwater drilling operations, the report said.

Administration officials promised an immediate response to the N.A.E. report, including regulations to set new standards for blowout preventers by the end of 2012. Today, 16 months after that deadline and four years after the blowout, we still have not seen even proposed rules. Deepwater drilling continues in the gulf. New leases are being offered by the government and sold to energy companies each year. Yet the N.A.E. report warned that a blowout in deep water may not be controllable with current technology.<sup>104</sup>

We may have escaped another BP-style disaster as a result of this unconscionable regulatory delay, but if so, it has merely been a matter of luck. The American people deserve better.

## 8. Pipeline Safety

Oil and gas pipeline spills have long been a concern for the public but the situation has deteriorated significantly since 2010. Major pipeline incidents have occurred in communities across the country, including Marshall, Michigan; San Bruno, California; Allentown, Pennsylvania; Sissonville, West Virginia; Harlem, New York; Mayflower, Arkansas; two spills into the Yellowstone River; in South Dakota a few days ago; and too many more.

In response, Congress passed a critical new pipeline safety bill in 2011 that required the Pipeline and Hazardous Materials Safety Administration (PHMSA) to produce dozens of new pipeline safety rules. Unfortunately, after almost 5 years, the law has yet to make any pipelines safer or prevent any future pipeline spills. This is because a broken regulatory process has left PHMSA unable to finalize a single new major safety rule despite strict deadlines set out by Congress in the law. As Cal Weimer of the Pipeline Safety Trust told the House Committee on Transportation and Infrastructure, there are several factors that have made PHMSA's rulemaking process dysfunctional and ineffective. Most important is that PHMSA must meet a demanding and rigid cost-benefit analysis standard when producing new safety rules. This requirement stems from the 1996 re-authorization of the pipeline safety program and was part of a broader and concerted effort in the mid-1990s to codify Executive Order requirements from Presidents Reagan and Clinton regarding regulatory cost-benefit analysis. Twenty years later, the results of this effort are clear: rather than improving rulemaking at PHMSA, cost-benefit analysis has led to regulatory paralysis at the agency. Specifically, pipeline operators control the information PHMSA requires to meet its cost-benefit requirement and are reluctant to agree to new reporting requirements that would provide this information to PHMSA. This put PHMSA in the "catch 22"

<sup>104</sup> S. Elizabeth Birnbaum and Jacqueline Savitz, "The Deepwater Horizon Threat," New York Times, April 16, 2014, available at: [http://www.nytimes.com/2014/04/17/opinion/the-deepwater-horizon-threat.html?\\_r=0](http://www.nytimes.com/2014/04/17/opinion/the-deepwater-horizon-threat.html?_r=0).



of not being able to fix pipeline safety problems because it does not have the information to understand what and where the problems are at the outset. Making matters worse, PHMSA needs more resources and staff to meet its stringent cost-benefit requirement and often encounters delays entirely outside its control when its rules undergo excessively lengthy reviews at the Office of Information and Regulatory Affairs (OIRA).<sup>105</sup>

To illustrate the problems PHMSA encounters in meeting its cost-benefit mandate, one only has to look at PHMSA's inability to regulate rural natural gas gathering lines. These pipelines pose many of the same risks as transmission pipelines, but because they are located in rural areas outside of the jurisdiction of any federal or state pipeline safety jurisdiction, there is little to no collection of information with respect to these pipelines. Thus, it is nearly impossible for PHMSA to pass regulations on rural natural gas gathering lines because PHMSA is unable to determine, much less quantify, the costs and benefits of the regulation.

**Remedies:** There needs to be much more Congressional oversight of rulemaking delay. The agencies appear to treat congressionally mandated deadlines for the issuance of new rules as suggestions rather than duties; it is up to Congress to hold them accountable.

The problem of industry exercising inappropriate influence at regulatory agencies, or even through the White House, is not easily cured. One important step to help would be new legislation to slow the revolving door between regulatory agencies and regulated parties. When agency officials and staff slide back-and-forth between working for the public and working on behalf of regulated parties, it's only natural that they will be overly sympathetic to industry when in public service, more deferential to requests for delay and less urgent in their advocacy for the public interest. The revolving door is a fundamental feature of the regulatory state. A recent report from the Project on Government Oversight (POGO) highlighted the pervasiveness of the problem at one agency, the Securities and Exchange Commission, finding that "from 2001 through 2010, more than 400 SEC alumni filed almost 2,000 disclosure forms saying they planned to represent an employer or client before the agency." And those disclosures, POGO notes, "are just the tip of the iceberg, because former SEC employees are required to file them only during the first two years after they leave the agency."<sup>106</sup>

Appropriate statutory reform would require longer cooling off periods before ex-agency staff can lobby their former agency for pecuniary purposes, broader definitions of what constitutes lobbying activity, strong rules against the reverse revolving door (persons moving from regulated industry employment to regulating agencies) and with high standards for any exceptions.

OIRA-caused delay is a less significant problem than earlier in the Obama administration, but reforms are necessary to ensure the agency does not contribute to delay or inappropriately

<sup>105</sup> Cal Weiner, Pipeline Safety Trust, testimony on "Reauthorization of DOT's Pipeline Safety Program, before the Subcommittee on Railroads, Pipelines and Hazardous Materials of the Committee on Transportation and Infrastructure, February 25, 2015, available at: <http://transportation.house.gov/uploadedfiles/2016-02-25-weiner.pdf>.

<sup>106</sup> Project on Government Oversight. (2013, February 11.) Dangerous Liaisons: Revolving Door at SEC Creates Risk of Regulatory Capture. Available from: <<http://pogoarchives.org/ebooks/20130211-dangerous-liaisons-sec-revolving-door.pdf>>.

weaken rules. OIRA processes are closed and non-transparent.<sup>107</sup> What is known is that OIRA meetings with outside parties are dominated by regulated industries (with industry meetings five times more prevalent than those with public interest groups), and that meetings correlate with changes in rules.<sup>108</sup> If OIRA is going to continue to its current function, it must be subject to much more transparency requirements. For example, agencies should put in the rulemaking docket all documents submitted to OIRA, and all changes and comments that they receive on proposed and/or final rules from OIRA or other agencies.

Most importantly, Congress must not act to make the problem of regulatory delay worse. In recent years, there have been numerous legislative proposals to further hinder agencies' abilities to do their jobs, imposing vast new analytic requirements on agencies and increasing the scope of OIRA authority. To review the record of persistent regulatory delay—and to recognize the degree to which current analytic requirements are responsible for that delay—is to understand how misguided these proposals are, and how serious would be their consequences. Many of these proposals would require agencies to perform new and additional cost-benefit analyses, a particularly flawed approach which I discuss in more detail below.

## **B. Strengthening regulatory enforcement**

In general, it is fair to say that the inspection agencies are understaffed and under-resourced.

Nowhere is the shortfall of inspectors more glaring than in the workplace safety and health area. "The federal Occupational Safety and Health Administration (OSHA) and the state OSHA plans have a total of 1,882 inspectors (8947 federal and 1,035 state inspectors) to inspect the 8 million workplaces under the OSH Act's jurisdiction," according to an AFL-CIO analysis. "This means there are enough inspectors for federal OSHA to inspect workplaces once every 140 years, on average, and for state OSHA plans to inspect workplaces once every 91 years."<sup>109</sup> Our nation's workers deserve better.

To take another example among many, there is general agreement that the Food and Drug Administration (FDA) does not have sufficient resources to meet its statutorily mandated responsibilities to ensure the safety of drugs and medical products, including through inspection of overseas plants. "Our current examination of FDA's resources confirms that the agency's ability to protect Americans from unsafe and ineffective medical products is compromised," the GAO recently found.<sup>110</sup> GAO explained that "[t]he structure of the agency's funding—its reliance on user fees to fund certain activities, particularly those related to the review of new products—is

<sup>107</sup> Government Accountability Office. (2009, April.) *Federal Rulemaking: Improvements Needed to Monitoring and Evaluation of Rules Development as Well as to the Transparency of OMB Regulatory Reviews*. Available from: <<http://www.gao.gov/new.items/d09205.pdf>>.

<sup>108</sup> Steinzor, R., Patoka, J. and Goodwin, J. Behind Closed Doors at the White House: How Politics Trumps Protection of Public Health, Worker Safety and the Environment. Center for Progressive Reform. 2011. Available from: <[http://www.progressivereform.org/articles/OIRA\\_Meetings\\_1111.pdf](http://www.progressivereform.org/articles/OIRA_Meetings_1111.pdf)>.

<sup>109</sup> AFL-CIO. (2015, April.) Death on the Job: The Toll of Neglect. p. 1. Available from: <<http://www.aflcio.org/content/download/154671/3868441/DOJ2015Finalnobug.pdf>>.

<sup>110</sup> Government Accountability Office. (2009, June.) Food and Drug Administration: *FDA Faces Challenges Meeting Its Growing Medical Product Responsibilities and Should Develop Complete Estimates of Its Resource Needs*. p.34. Available from: <<http://www.gao.gov/new.items/d09581.pdf>>.

a driving force behind which responsibilities FDA does and does not fulfill. The approval of new products has increasingly become the beneficiary of the agency's budget, without parallel increases in funding for activities designed to ensure the continuing safety of products, once they are on the market."

Of course, the issue with adequate enforcement is not solely a matter of resources. Many agencies do an inadequate job of enforcing rules due less to resource limitations than issues involving allocation of resources, prioritization and/or insufficient rigor. The 2013 fungal meningitis outbreak, for example, could and should have been prevented by FDA. The agency issued a warning letter to the New England Compounding Center in 2006, instructing the company to stop manufacturing-scale operations. However, FDA failed to follow up adequately. For whatever reason, whether inattentiveness or lack of compliance and legal resources, by not aggressively enforcing the regulations related to drug manufacturing and interstate commerce, the FDA allowed the company to continue its wide-scale manufacturing and interstate distribution operation of multiple high-risk drugs, including injectable steroids. The eventual result was the meningitis outbreak and 48 deaths.<sup>111</sup>

The GM ignition switch debacle provides another example of regulatory failure—resulting in at least 111 deaths, and climbing. What is unique here is that the agency, now under new leadership, acknowledges its failures. A recent NHTSA report blames GM for its horrible misconduct, but also assigns major responsibility to NHTSA itself.<sup>112</sup> The report's major findings:

- GM withheld critical information about engineering changes that would have allowed NHTSA to more quickly identify the defect.
- NHTSA did not hold GM accountable for providing inadequate information.
- Neither GM nor NHTSA completely understood the application of advanced air bag technology in GM vehicles.
- NHTSA did not consider alternate theories proposed by internal and external sources.
- NHTSA did not identify and follow up on trends in its own data sources and investigations.

**Remedies:** The agency resource problem is easily solved with sufficient political will, though budget tightening efforts have cramped rather than expanded enforcement budgets. This is surely a penny wise but pound foolish approach. In areas where regulators are able to apply stiffer penalties, they may be able to bring more money into the treasury than they expend. Far more important is the social cost accounting: the economic benefits of properly enforced laws vastly exceed costs. This is most obviously true in the financial sector, as the discussion earlier regarding the Great Recession and regulatory failure elaborates, but it is true in virtually all areas. The economic benefits of reducing food contamination through inspection and regulatory enforcement, for example, vastly exceed costs. Indeed, if regulatory budgets were set based on

<sup>111</sup> See Carome, M. and Wolfe, S. (2012, October 24.) Letter to Secretary of Health and Human Services Kathryn Sebelius. Available from: <<http://www.citizen.org/documents/2080.pdf>>.

<sup>112</sup> Department of Transportation (2015). NHTSA's Path Forward. Available from: <<http://www.nhtsa.gov/About+NHTSA/Press+Releases/nhtsa-forming-new-safety-teams>>.

the kind of cost-benefit analyses that are applied to new regulation, they would be dramatically larger.

Ensuring a sufficiently robust enforcement culture at regulatory agencies is not a problem that lends itself to a simple solution, though and stronger Congressional oversight of agency enforcement would go a long way. The NHTSA example of critical self-reflection in the wake of horrendous failure—a major change for the agency—should be monitored, studied and, assuming it does generate a change in the culture and practice at the agency, emulated.

### C. An Appropriate Role for Cost-Benefit Analysis

Whatever the benefits of cost-benefit analysis as a tool to assist in regulatory decision-making, it should be recognized that cost-benefit analysis is highly imperfect and, at least as implemented in the real world, suffers from a set of flaws that tend to systematically skew in favor of regulated parties and against the broader public interest, by overestimating costs and underestimating benefits. Even ardent supporters of cost-benefit analysis, such as Cass Sunstein, the former OIRA administrator, argue that cost-benefit analysis is more appropriate as a guidance tool for agencies, rather than as a definitive metric directing agencies into a particular course of action.<sup>113</sup> As such, it would be a mistake to require any additional cost-benefit analysis in the regulatory system, or to give it a more prescriptive role in regulatory decision making.

The problems with cost-benefit analysis are legion.

First, regulated industry typically has an undue influence over cost estimates, in large part because it controls access to internal corporate information, as well as because of its ability to commission studies that tend to support the interest of their funders. This information asymmetry is a significant problem in the conduct of cost-benefit analysis, including because businesses may not provide important cost information or disclose methodological assumptions in their submitted cost estimates.<sup>114</sup>

It should not be controversial to recognize that corporations have a natural bias to overestimate cost of rules that may affect the way they conduct business. As a result, while there is a long history of industry claiming that the next regulation under consideration would unreasonably raise the cost of doing business, those claims routinely prove to be overblown.

- Bankers and business leaders described the New Deal financial regulatory reforms in foreboding language, warning that the Federal Deposit Insurance Commission and related agencies constituted "monstrous systems," that registration of publicly traded securities constituted an "impossible degree of regulation," and that the New Deal reforms would

<sup>113</sup> U.S. Senate Comm. on Homeland Sec. and Governmental Affairs, Pre-hearing Questionnaire for the Nomination of Cass R. Sunstein to Be Administrator of the Office of Information and Regulatory Affairs, p. 5. Available from: <[http://www.ombwatch.org/files/regs/PDFs/Sunstein\\_questions.pdf](http://www.ombwatch.org/files/regs/PDFs/Sunstein_questions.pdf)>. ("[C]ost-benefit analysis is a tool meant to inform decisions; it should not be used to place regulatory decisions in an arithmetic straightjacket").

<sup>114</sup> Ruttenberg, R. (2004). Not Too Costly, After All: An Examination of the Inflated Cost Estimates of Health, Safety and Environmental Protections. Available from <<https://www.citizen.org/documents/ACF187.pdf>>.

"cripple" the economy and set the country on a course toward socialism.<sup>115</sup> In fact, those New Deal reforms prevented a major financial crisis for more than half a century—until they were progressively scaled back.

- Chemical industry leaders said that rules requiring removal of lead from gasoline would "threaten the jobs of 14 million Americans directly dependent and the 29 million Americans indirectly dependent on the petrochemical industry for employment." In fact, while banning lead from gasoline is one of the single greatest public policy public health accomplishments, the petrochemical industry has continued to thrive. The World Bank finds that removing lead from gasoline has a ten times economic payback.<sup>116</sup>
- Big Tobacco long convinced restaurants, bars and small business owners that smokefree rules would dramatically diminish their revenue—by as much as 30 percent, according to industry-sponsored surveys. The genuine opposition from small business owners—based on the manipulations of Big Tobacco—delayed the implementation of smokefree rules and cost countless lives. Eventually, the Big Tobacco-generated opposition was overcome, and smokefree rules have spread throughout the country—significantly lowering tobacco consumption. Dozens of studies have found that smokefree rules have had a positive or neutral economic impact on restaurants, bars and small business.<sup>117</sup>
- Rules to confront acid rain have reduced the stress on our rivers, streams and lakes, fish and forests.<sup>118</sup> Industry projected costs of complying with acid rain rules of \$5.5 billion initially, rising to \$7.1 billion in 2000; ex-ante estimates place costs at \$1.1 billion to \$1.8 billion.<sup>119</sup>
- In the case of the regulation of carcinogenic benzene emissions, "control costs were estimated at \$350,000 per plant by the chemical industry, but soon thereafter the plants developed a new process in which more benign chemicals could be substituted for benzene, thereby reducing control costs to essentially zero."<sup>120</sup>
- The auto industry long resisted rules requiring the installation of air bags, publicly claiming that costs would be more than \$1000-plus for each car. Internal cost estimates actually showed the projected cost would be \$206.<sup>121</sup> The cost has now dropped

<sup>115</sup> Lincoln, T. (2011). *Industry Repeats Itself: The Financial Reform Fight*. Public Citizen. Available from: <<http://www.citizen.org/documents/Industry-Repeats-Itself.pdf>>.

<sup>116</sup> Crowther, A. (2013). *Regulation Issue: Industry's Complaints About New Rules Are Predictable -- and Wrong*. p.8. Available from: <<http://www.citizen.org/documents/regulation-issue-industry-complaints-report.pdf>>

<sup>117</sup> *Regulation Issue: Industry's Complaints About New Rules Are Predictable -- and Wrong*. p.10.

<sup>118</sup> Environmental Protection Agency. *Acid Rain in New England: Trends*. Available from: <<http://www.epa.gov/region1/eco/acidrain/trends.html>>.

<sup>119</sup> The Pew Environment Group. (2010, October). *Industry Opposition to Government Regulation*. Available from: <[http://www.pewenvironment.org/uploadedFiles/PEG/Publications/Fact\\_Sheet/Industry%20Clean%20Energy%20FactSheet.pdf](http://www.pewenvironment.org/uploadedFiles/PEG/Publications/Fact_Sheet/Industry%20Clean%20Energy%20FactSheet.pdf)>.

<sup>120</sup> Shapiro, I., & Irons, J. (2011). *Regulation, Employment, and the Economy: Fears of job loss are overblown*. Economic Policy Institute. Available from <<http://www.epi.org/files/2011/BriefingPaper305.pdf>>.

<sup>121</sup> Behr, P. (August 13, 1981). U.S. Memo on Air Bags in Dispute. Washington Post.

significantly below that. The National Highway Traffic Safety Administration estimates that air bags saved 2,300 lives in 2010, and more than 30,000 lives from 1987 to 2010.<sup>122</sup>

There is a long list of other examples from the last century—including child labor prohibitions, the Family Medical Leave Act, the CFC phase out, asbestos rules, coke oven emissions, cotton dust controls, strip mining, vinyl chloride<sup>123</sup>—that teach us to be wary of Chicken Little warnings about the costs of the next regulation.

Second, cost-benefit analyses tend to include static estimates of cost, based on existing technologies and business systems. But industry and our national economy is characterized by technological dynamism, and compliance costs regularly fall quickly once new rules are in place. Many of the examples above—from benzene to air bags—illustrate this point, and there are many other examples. Indeed, regulation spurs innovation and can help create efficiencies and industrial development wholly ancillary to its directly intended purpose.

Looking at a dozen emissions regulations in 1997, Hodges found that early estimates of cost were at least double subsequent estimates or actually realized costs. (Interestingly, the Hodges study found that while emissions reductions estimated or actual costs fell dramatically over time, costs for clean-up typically exceeded estimates—underscoring the case for preventative regulation.)<sup>124</sup>

“Part of the reason for the error” of repeated overestimations of regulatory cost,” Hodges found “is that, over time, process and product technologies change. An estimate of the cost of compliance with a particular regulation might be based on one technology while actual compliance costs are based on another.” Once business must respond to implemented regulations, they stop bemoaning them and work to do so as efficiently as possible; technological innovation, learning by doing, and economies of scale routinely cut costs far below initial estimates.<sup>125</sup>

A decade ago, in a detailed report prepared for Public Citizen, Ruttenberg cited a series of factors that explained how technological dynamism led to actual costs far below those estimated in cost-benefit analysis:

- Cost-benefit analyses routinely exhibit inaccurate assumptions about the compliance path industry actually follows once new standards are in place;

<sup>122</sup> National Highway Traffic Safety Administration. (2012). Traffic Safety Facts: Occupant Protection. Available from: <<http://www.nrd.nhtsa.dot.gov/Pubs/811619.pdf>>.

<sup>123</sup> *Regulation Issue: Industry's Complaints About New Rules Are Predictable -- and Wrong*; Hodges, H. (1997). *Falling Prices: Cost of Complying With Environmental Regulations Almost Always Less Than Advertised*. Economic Policy Institute. Available from: <<http://www.epi.org/publication/bp69>>; Shapiro, I., & Irons, J. (2011). *Regulation, Employment, and the Economy: Fears of job loss are overblown*. Economic Policy Institute. Available from: <<http://www.epi.org/files/2011/BriefingPaper305.pdf>>.

<sup>124</sup> Hodges, H. (1997). *Falling Prices: Cost of Complying With Environmental Regulations Almost Always Less Than Advertised*. Economic Policy Institute. Available from: <<http://www.epi.org/publication/bp69>>

<sup>125</sup> Hodges, H. (1997). *Falling Prices: Cost of Complying With Environmental Regulations Almost Always Less Than Advertised*. Economic Policy Institute. Available from: <<http://www.epi.org/publication/bp69>>

- Cost-benefit analyses regularly fail to consider new adaptations of existing technologies to meet new standards;
- Cost-benefit analyses generally do not consider the positive effects of learning by doing and economies of scale;
- Cost-benefit analyses often fail to considering adaptations to technology already in place in other industries; and
- Cost-benefit analyses typically fail to account for new innovations that follow from new regulatory standards.<sup>126</sup>

Ruttenberg highlights the case of vinyl chloride as an illustrative case study. When OSHA began developing a new health standard to reduce the risk of workers developing liver cancer, the industry claimed that the new standard threatened to “shut down” the industry and estimated costs on the order of \$65-90 billion. Once the standard was in place, industry quickly implemented six technological changes—ranging from improved housekeeping to reduce exposures to new computerized production processes that reduced exposures and saved money—within 18 months. Retrospective analyses of costs placed them at far below 1 percent of industry’s pre-rule analyses, with actual costs placed at between \$25 million to \$182 million, depending on how costs are calculated.<sup>127</sup>

Third, although numerous business trade association papers suggest to the contrary, capital-intensive compliance costs do not continue to accumulate in perpetuity. When a new standard is in place, industry invests in improvements or new capital equipment to comply with new rules, after which costs are generally not recurring. (There are, to be sure, ongoing compliance costs in some instances, notably for ongoing reporting requirements, but those typically do not involve costs at the scale of regulations requiring significant capital investments.) One piece of evidence in this regard is that while industry regularly and aggressively contests new rules, at least in the health, safety and environmental areas, it does not continue to complain about rules once they are well established.<sup>128</sup>

Fourth, claims of precision notwithstanding, cost-benefit analysis is open to bizarre and second- and third-order accounting, in practice especially on the cost side. One deeply troubling example of bizarre cost-accounting is the “lost pleasure principle,” an application of “consumer surplus” theory. Under this theory, when a regulation takes away an option from consumers or makes it less likely they will choose an option they would have in the absence of the regulation, cost-benefit analysis should take into account the resulting “lost pleasure.” This is not the kind of factor that proponents of cost-benefit analysis would normally factor on the benefit side, to say the least, as I discuss further below. But they urge it be considered on the cost side. And the value they attribute to this purported cost can be extraordinarily high, since they impute the price

<sup>126</sup> Ruttenberg, R. (2004). Not Too Costly, After All: An Examination of the Inflated Cost Estimates of Health, Safety and Environmental Protections. Available from <<https://www.citizen.org/documents/ACF187.pdf>>. pp 22-32.

<sup>127</sup> Ruttenberg, R. (2004). Not Too Costly, After All: An Examination of the Inflated Cost Estimates of Health, Safety and Environmental Protections. Available from <<https://www.citizen.org/documents/ACF187.pdf>>. pp 32-33.

<sup>128</sup> Lincoln, T. (2014, September 16.) Streamlining the Rules-Making Process. The Hill. Available from: <<http://thehill.com/blogs/congress-blog/the-administration/217751-streamline-the-rules-making-process>>.

that consumers were willing to pay for the product pre-regulation as the cost (multiplied by number of purchases).<sup>129</sup>

Confoundingly, some economists have even argued for application of the lost pleasure principle when regulations lead consumers to make new choices simply based on new information; one would actually anticipate that consumer welfare increases when consumers are better informed and make choices accordingly, with no diminution in consumer “pleasure.” If I choose to eat apples instead of apple pie because nutrition labeling has educated me on the health impact of eating too much apple pie, it hardly makes sense to say a regulation has cost me pleasure. I’ve made my own choice, based on regulation helping me better understand my choices.

Yet actual economists doing cost-benefit analysis that helps establish new government rules have employed exactly this Through-the-Looking-Glass logic. They have done so even in the case of an addictive product, cigarettes,<sup>130</sup> where there is a new layer of absurdity because most adult users actually say they would like to stop using it.<sup>131</sup>

Against all measures of common sense, these economists for a time succeeded in applying the lost pleasure principle to food labeling and tobacco regulations. After an ensuing public controversy—and deep concern expressed by a number of Senators—the Department of Health and Human Services scaled back, at least for now, use of the lost pleasure principle.<sup>132</sup> Thus, it appears that the ongoing outrage of the lost pleasure principle interfering with proper standard setting—at least in the consumer health area—has been alleviated, for now. But the serious suggestion of such an approach, which was held to reduce benefits by as much as 70-90 percent in some cases, shows how easy it is to manipulate cost-benefit analysis, and underscores the massive imprecision in cost-benefit exercises.

Fifth, cost-benefit analysis systematically underestimates benefits. New regulatory costs can—and should—also be considered benefits in many cases. That is, costs to regulated businesses are not the same as social costs. New productive capital investment helps create new demand, creates new jobs, and helps spur new technology. These benefits are rarely captured in cost-benefit analyses, in part because they are uncertain, in part because they appear to be second-order effects (even though they are the mirror image of direct costs). Yet these benefits are significant, which is why the actual impact on employment of consumer, health, safety and

<sup>129</sup> See Ashley, E., Nardinelli, C. and Lavaty, R. (2015.) Estimating the Benefits of Public Health Policies that Reduce Harmful Consumption. 24 *Health Economics* 5, 617-624.

<sup>130</sup> See Begley, S. (2014, June 2.) FDA Calculates Costs of Lost Enjoyment if E-cigarette Rules Prevent Smoking. Reuters. Available from: <<http://www.reuters.com/article/2014/06/02/us-fda-tobacco-insight-idUSKBN0ED0A620140602>>.

<sup>131</sup> See Chaloupka, F. et. al. (2014, December 30.) An evaluation of the FDA's Analysis of the Costs and Benefits of the Graphic Warning Label Regulation. Tobacco Control. 10.1136/tobaccocontrol-2014-052022; Song, A., Brown, P., Glantz, S. (2014, May 30). Comment on the Inappropriate Application of a Consumer Surplus Discount in the FDA's Regulatory Impact Analysis, Docket No. FDA-2014-N-0189. Available from: <<https://tobacco.ucsf.edu/sites/tobacco.ucsf.edu/files/u9/FDA-comment-consumer-surplus-May30-%201jy-8cdp-qb60.pdf>>.

<sup>132</sup> Begley, S. and Clarke, T. (2015, March 18.) U.S. to Roll Back “Lost Pleasure” Approach on Health Rules. Reuters. Available from: <<http://www.reuters.com/article/2015/03/18/us-usa-health-lostpleasure-idUSKBN0ME0DD20150318>>.



environmental regulation is far less than anti-regulatory forces claim and in many cases may well register a net zero or positive impact.

Cost-benefit analysis also systematically underestimates benefits because of its insistence on, or at least strong bias in favor of, monetization. Yet health, safety, consumer, environmental, employment and similar regulatory protections yield benefits that are not easily monetized; and attempts to translate these benefits into monetary terms almost always fall short of capturing the full range of improvements they afford to our standard of living. The benefits of not losing an arm, of not choking for air when breathing, of not dying a painful and early death from cancer, of not feeling the stress of debt collector calls or the prospect of losing your home go far beyond what can be captured in a dollar figure. So too many other benefits of regulation—enhanced privacy, dignity, equality, freedom and liberty, fairness, community, a functioning democracy and many others—evade easy capture by a dollar figure.

What is the price tag on the pain a parent feels when they back their car over their child? That's not easily answered, but surely the benefit of preventing that pain is real. But such considerations generally do not merit inclusion in official cost-benefit analyses.

When Congress directs the Department of Justice to eliminate prison rape but to avoid “substantial additional costs,” should the government also conduct a cost-benefit analysis reliant in part on what victims would be willing to pay to avoid rape? It is common sense that the answer is no, but this actually occurred. Morally revolting on its face, Georgetown University Professor Lisa Heinzerling lays bare the logic of this exercise: “In the strange logic and twisted morality of cost-benefit analysis, the victim—not the perpetrator—must be willing to pay up to avoid the crime.” She adds, pointedly, that “rape is a serious crime, not a market transaction” and “that framing rape as a market transaction strips it of the coercion that defines it.”<sup>133</sup>

Last, and related to the previous point, while perhaps it is unavoidable in some areas of public policy, the idea of placing a dollar value on a human life should, at minimum, be approached with great humility—an attribute one would not normally associate with the practitioners of cost-benefit analysis.

Two years ago, 8 men and women were killed in an Amtrak crash near Philadelphia.<sup>134</sup> The National Transportation Safety Board says that crash could have been prevented if Positive Train Control technology had been in place, as the NTSB has long advocated. Yet although the NTSB has urged adoption of the technology since 1970, and although Congress in 2008 mandated that all railroads deploy the technology by December 31, 2015, this objective was not met. (Amtrak appears to be ahead of most railroads in deployment.) There are plainly many factors accounting for the delay in meeting the Congressional mandate. But it may be that one reason for that

<sup>133</sup> Heinzerling, L. (2012, June 14.) Cost-Benefit Jumps the Shark: The Department of Justice's Economic Analysis of Prison Rape. Available from: <<http://www.progressivereform.org/CPRBlog.cfm?idBlog=EB3B070D-F7A0-1489-B361DA6B35ABC16E>>.

<sup>134</sup> AP. (2014, May 14.) All 8 Fatal Victims in Amtrak Crash Identified. Available from: <<http://6abc.com/news/all-8-fatal-victims-in-amtrak-crash-idd/719973>>.

regulatory delay was that some officials believed that the regulatory standard was not cost effective.<sup>135</sup>

That was easy enough to say when the deaths averted were just statistical abstractions. Now, with the horrible and apparently preventable deaths of identifiable human beings, things are dramatically different. The cost-benefit-analysis-influenced delay of the implementation of Positive Train Control technology now seems callous, cruel and fundamentally wrong—and it was. But all that has changed is we now replace statistical abstractions with human compassion.

**Remedies:** Decision makers should recognize that cost-benefit analysis is a flawed analytic tool that may be of some assistance on some occasions, but not one that should be determinative in the rulemaking process. At bare minimum, Congress should not act to impose new cost-benefit analytic requirements on agencies, or to make cost-benefit determinations more controlling.

#### **D. Imbalanced and inappropriate judicial review**

Judicial review of agency action is an important and necessary part of our administrative process and general system of checks and balances, but judicial review of rulemakings has gone awry. Most major rules are challenged in court upon issuance, and lengthy challenges by regulated parties are standard. One significant problem is that there is a major imbalance in the ability of regulated parties and the public to challenge rules (or the failure to issue rules) on procedural or substantive grounds. A second major problem is the misguided importation by courts of cost-benefit requirements into review of agency action. There are other problems related to judicial review of agency action, notably an overly expansive view of corporate First Amendment speech rights, that are beyond the purview of this testimony, but worth noting.

##### **1. Imbalanced rights to challenge agency action: the standing problem.**

On behalf of consumers and the public whom all regulation is ultimately intended to benefit, Public Citizen has brought numerous challenges to agency regulations during our almost 45-years of work. The challenges are an important tool for ensuring that agencies adhere to statutory requirements and make rational decisions based on the available information. Over the past 20 or so years, however, a series of unduly narrow standing decisions have impeded our ability, and the ability of litigants representing the broad public interest, to obtain judicial redress for unlawful agency action that will cause them injury.

The Supreme Court's and DC Circuit's standing decisions aim to confine the federal courts to their legitimate function of resolving "actual cases or controversies" and "to prevent the judicial process from being used to usurp the powers of the political branches."<sup>136</sup> But in too many cases, a court has denied standing to parties who are threatened with "certainly impending" injuries that are "fairly traceable" to an agency's action,<sup>137</sup> —even action that they claim violates a clear

<sup>135</sup> See Mann, T. (2013, June 17.) Rail Safety and the Value of a Life. Wall Street Journal. Available from: <http://www.wsj.com/articles/SB10001424127887323582904578485061024790402>; Freedman, D. (2015, May 18.) Obama Official Once Said Train-Safety Cost Outweighed Benefit. Connecticut Post. Available from: <http://www.ctpost.com/local/article/Obama-official-once-said-train-safety-cost-6271486.php>.

<sup>136</sup> *Clapper v. Amnesty Int'l USA*, 133 S. Ct. 1138, 1147 (2013).

<sup>137</sup> *Clapper v. Amnesty Int'l USA*, 133 S. Ct. 1138, 1143 (2013).

statutory limit on the agency's authority. In these cases, to dismiss the case for lack of standing constitutes an abdication of the judicial function of deciding cases. That abdication is all the more serious when, as has happened in several cases, it prevents adjudication of a legal issue that has profound national consequences.

To be sure, "generalized grievances" are not a basis for standing.<sup>138</sup> And we do not suggest that the fact that a regulation or policy may be harmful means that the particular parties challenging it necessarily have standing. By the same token, the fact that a policy causes concrete harms to a many members of the public does not mean that each of those persons do not have standing to challenge it.<sup>139</sup>

For example, in one case, the DC Circuit's very narrow view of standing barred litigation of challenge to a NHTSA rule setting the standard for tire pressure monitoring systems that Congress directed the agency to make driving safer. Although the standard was intended for the benefit of the public, that court held that Public Citizen did not have standing to challenge it on behalf of our members (all at some point vehicle owners, drivers, passengers, or pedestrians) unless we could show statistically that the agency's rule presented a substantially increased risk of harm to consumers and that the ultimate risk is substantial. In addition, the court said that because the injury alleged was based on the government's regulation of automakers, not regulation of Public Citizen members, to demonstrate standing we had to show that causation did not depend on choices made by the automakers. Specifically, we were instructed to show that automakers would not voluntarily exceed the safety standard that NHTSA adapted; that drivers would not seek to prevent injury to themselves or to other people by manually checking their tires and then inflating them properly; and to show that drivers will pay attention to the warning light that will be installed in cars. Not only had two of these topics had been addressed specifically in the Federal Register notices that accompanied issuance of both rules, but the court's instruction effectively questioned the conclusions of Congress in enacting the law requiring NHTSA to require these monitoring devices.

When Congress has addressed the matter that is the subject of our suit and the agency failed to do what Congress asked it to do, the courts are an appropriate and proper place to hold the executive branch accountable for failure to abide by the law. It is simply not practicable or desirable to expect Congress to revisit the issue each time the agency does not live up to the legislative mandate. Congress, through the Administrative Procedure Act and statutes that authorize judicial review of agency actions, has confirmed that courts can and should entertain such suits. That does not mean that a plaintiff or a petitioner does not need to have stake in the case, because, after all, the case or controversy requirement comes from the Constitution, not from Congress. Once Congress has spoken, however, and the agency has acted, the courts have an important role to play.

What is crucial to emphasize is that judicially created standing doctrine does not affect all parties evenly; instead, it creates a structural advantage for the corporate sector. In general, the courts typically hold that regulated parties have standing to challenge agency action. In contrast, organizations and individuals seeking to realize rights and protections conferred by Congress

<sup>138</sup> *Lance v. Coffman*, 549 U.S. 437, 439 (2007).

<sup>139</sup> *See Federal Election Comm'n v. Akins*, 524 U.S. 11, 24-25 (1998).

face much greater difficulties; under the case law, it is not uncommon that no person or individual is deemed to have standing to enforce agency compliance with congressional directives.

## 2. Judicially imposed requirements of cost-benefit analysis.

The relationship between Congress, the regulatory agencies and the courts is a complicated one, not subject to simple formulaic rules about appropriate level of judicial deference to agency action. On the one hand, it is appropriate for the courts to ensure agencies are faithful to Congressional directives. On the other hand, the courts need show deference to the technical expertise of agencies, which are designed to convert broad Congressional directives into concrete rules. Judges should not abrogate well-crafted rules, nor invent requirements for rules to be justified by cost-benefit tests that are not statutorily required.

Yet as cost-benefit analysis has intruded deeper into the rulemaking process, courts have begun to subject these analyses to scrutiny, or to impose their own cost-benefit requirements on agency decision making. Because of the inherent imprecision of cost-benefit analysis, and because of relative institutional strengths, courts should subject agency cost-benefit analyses to no or exceedingly deferential review and should not impose cost-benefit requirements on agencies.

*Business Roundtable v. SEC*<sup>140</sup> is a case that highlights the concern about courts and cost-benefit analysis. In *Business Roundtable*, the D.C. Circuit struck down rule 14a-11 (the "proxy access rule"). Adopted by the SEC pursuant to authority under the Dodd-Frank Act, the rule would have allowed long-term shareholders to include nominees for the board of directors in a publicly traded company's proxy statement. Without such a right, shareholders in most instances have no realistic means of running candidates for director against management-selected candidates.

The D.C. Circuit held that the SEC had failed to meet its "unique obligation"<sup>141</sup> to analyze rules for their impact upon "efficiency, competition, and capital formation"<sup>142</sup> under Section 3(f) of the Exchange Act,<sup>143</sup> thereby rendering the SEC's promulgation of the rule "arbitrary and capricious."<sup>144</sup> Yet, nothing in the relevant legislative history indicates that Congress intended for the SEC's economic analyses relating to "efficiency, competition, and capital formation" to be akin to full blown cost-benefit analysis or take precedence over the SEC's primary mission to protect investors.<sup>145</sup> Nonetheless, in a string of recent cases,<sup>146</sup> the D.C. Circuit has interpreted this language as imposing a duty on the SEC to fully assess the costs and benefits of their regulations and determine, in some instances, that the regulation yields a "net benefit."<sup>147</sup> In the *Business Roundtable* opinion, the D.C. Circuit lambasted the SEC for "having failed once again

<sup>140</sup> *Business Roundtable v. SEC* 647 F.3d 1144 (D.C. Cir. 2011).

<sup>141</sup> *Business Roundtable v. SEC*, 1148.

<sup>142</sup> *Business Roundtable v. SEC*, 1148.

<sup>143</sup> 15 U.S.C. §§ 78c(f), 78w(a)(2), 80a-2(c).

<sup>144</sup> *Business Roundtable v. SEC*, 1155.

<sup>145</sup> See Generally James D. Cox and Benjamin J.C. Baucom, *The Emperor Has No clothes: Confronting the D.C. Circuit's Usurpation of SEC Rulemaking Authority*, 90 Tex. L. Rev 1811 (2012).

<sup>146</sup> *Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005); *American Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166 (D.C. Cir. 2010).

<sup>147</sup> *Business Roundtable v. SEC*, 1153.

... adequately to assess the economic effects of a new rule"<sup>148</sup> by having "inconsistently and opportunistically framed the costs and benefits of the rule; failed adequately to quantify certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgment; contradicted itself; and failed to respond to substantial problems raised by commenters."<sup>149</sup>

Several features of the decision are remarkable. First, the SEC was acting pursuant to specific Dodd-Frank-conferred power, which authorized the agency to adopt a rule requiring "that a solicitation of proxy, consent, or authorization by (or on behalf of) an issuer include a nominee submitted by a shareholder to serve on the board of directors of the issuer."<sup>150</sup> This fact was unmentioned in the court's decision, and earned the agency no deference. Second, the court failed to address the fact that the benefit of advancing shareholder democracy is inherently non-quantifiable. Third, the extraordinarily intrusive review of agency decision-making included a challenge to the benefit of shareholder democracy—a value that one might think speaks for itself, but in any case was clearly the underlying objective of Congress in authorizing the SEC to issue a proxy access rule.<sup>151</sup>

**Remedies:** *Business Roundtable* has cast a shadow over Dodd-Frank and other agency rulemaking, making agencies fearful and reluctant to proceed with rulemakings. Congress should act to establish clearer and more deferential standards of judicial review where agencies are acting in response to specific Congressional directives, and as regards cost-benefit analysis, and should make clear that courts are not to impose their own cost-benefit tests on agency action.

#### E. Regulation to assist small business and promote competitive markets

Much of the regulatory policy debate over the last couple years has misleadingly focused on the impact of regulation on small business, with regulation critics claiming that regulation poses unreasonable burdens on small business. In surveys and poll data, small businesses generally do not agree with their purported advocates. They cite inadequate demand and economic uncertainty as their biggest problems.<sup>152</sup> And regulatory law is replete with special and intentional protections for smaller firms, which are exempt from many rules.

What has been missing from the regulatory policy debate is a focus on the ways that regulation does—or should—assist small business in creating a level playing field.

<sup>148</sup> *Business Roundtable v. SEC*, 1148.

<sup>149</sup> *Business Roundtable v. SEC*, 1148-49.

<sup>150</sup> Section 971.

<sup>151</sup> *Business Roundtable v. SEC*. ("By ducking serious evaluation of the costs that could be imposed upon companies from use of the rule by shareholders representing special interests, particularly union and government pension funds, we think the Commission acted arbitrarily.")

<sup>152</sup> Small Business Majority. (2011). *Opinion Survey: Small Business owners Believe National Standards Supporting Energy Innovation Will Increase Prosperity for Small Firms*. Available from: <[http://smallbusinessmajority.org/energy/pdfs/Clean\\_Energy\\_Report\\_092011.pdf](http://smallbusinessmajority.org/energy/pdfs/Clean_Energy_Report_092011.pdf)>. Similarly, in a 2011 informal survey, McClatchy/Tribune News Service found no business owners complaining about regulation. Hall, K. G. (2011, 1 September). *Regulations, taxes aren't killing small business, owners say*. McClatchy Newspapers. Available from: <<http://www.mcclatchydc.com/2011/09/01/122865/regulations-taxes-arent-killing.html>>.

First, as a preliminary matter in this area, policymakers concerned about aiding small business might fruitfully focus on the issue of regulatory compliance. Small firms may on occasion have difficulty discerning what standards apply to them and what they must do to meet their obligations under various rules. There may be value in legislation encouraging agencies to conduct more outreach, education and compliance assistance to small businesses on their regulatory obligations. Agencies with Small Business Ombudsman offices could be tasked with ensuring that those offices are conducting effective regulatory outreach and education to small businesses. "Best practices" guidelines for federal agencies could be established, including those with Small Business Ombudsman offices, to follow when working to ease regulatory compliance for small businesses.

A larger area of Congressional focus should aim to address the problem that leading sectors of the economy are highly concentrated, and that widespread anti-competitive conduct unfairly disadvantages small business, while also hurting consumers and overall economic efficiency.

Congress and regulators should look to reinvigorate antitrust and competition policy. Action across a broad range of areas would very meaningfully advance small business success, and ensure smaller companies are not unfairly exploited, disadvantaged or eliminated by larger rivals.

- Large banks receive a massive implicit government subsidy thanks to the widespread market perception that these institutions are "too big to fail"—in other words, that protestations to the contrary, the government will in times of crisis bail out these giant banks to prevent a financial system meltdown. Because the market judges these institutions too big to fail, the giant banks are able to access capital at costs significantly below that are available to regular banks, as well as obtain other implicit subsidies. Various analysts place this benefit as ranging from tens of billions of dollars annually to more than \$100 billion, with the scale of the subsidy varying over time.<sup>153</sup>

**Remedies:** This subsidy plainly disadvantages smaller banks and credit unions, and is itself a compelling reason—there are many other such reasons—to break up the giant banks. At bare minimum, this goliath bank subsidy emphasizes the imperative of a financial sector competition policy that removes the unfair advantage giant firms obtain.

- Patent enforcement by patent acquiring entities—often known colloquially as "patent trolls"—imposes a significant tax on innovation, especially by small business. Enforcement actions and license fees by these entities are skyrocketing, now costing almost \$30 billion a year, with researchers finding only a quarter of this total flowing back to innovation.<sup>154</sup>

<sup>153</sup> See Federal Reserve of Minneapolis. (2013, November 18-19). Workshop: Quantifying the Too Big to Fail Subsidy. Available from: <<https://www.minneapolisfed.org/publications/special-studies/too-big-to-fail/quantifying-the-too-big-to-fail-subsidy>>. Bloomberg. (2013, Feb 20.) *Why Should Taxpayers Give Big Banks \$83 Billion a Year*. Available from: <<http://www.bloomberg.com/news/2013-02-20/why-should-taxpayers-give-big-banks-83-billion-a-year.html>>.

<sup>154</sup> See Leibowitz, J. (2012, Dec. 10.) Patent Assertion Entity Workshop: Opening Remarks. Federal Trade Commission. Available from: <<http://www.ftc.gov/speeches/leibowitz/121210paeworkshop.pdf>>; Skitol, R. (2012, Dec. 14.) FTC-DOJ Workshop on Patent Assertion Entity Activities: Fresh Thinking on Potential Antitrust

**Remedies:** Stronger rules should protect small business innovators, and innovative large corporations as well, from improper patent enforcement actions.

- Anticompetitive practices are widespread in the energy industry, including in electricity markets. "Anticompetitive agreements between sellers in regional wholesale electricity markets have forced consumers to pay hundreds of millions of dollars more for electricity than they would have in the absence of such conduct," notes the American Antitrust Institute's Diana Moss. "In these markets, which are structurally vulnerable to the exercise of market power, anticompetitive agreements spanning even a short time can result in large wealth transfers from consumers to suppliers."<sup>155</sup> Those consumers include small business.

Recently, enforcement against anticompetitive conduct by the Federal Electric Regulatory Commission has picked up considerably, with FERC notably suspending companies found to have lied to regulators and engaging in anticompetitive actions. However, the deregulated structure of electricity markets creates the potential for anticompetitive activity, and suggests the need for new rules to ensure competitive benefits are actually accruing.

Last year, for example, Public Citizen filed an emergency complaint at FERC<sup>156</sup> alleging that Houston-based Dynegy, Inc. may have intentionally withheld several of its power plants from a power auction conducted by the Midcontinent Independent System Operator (MISO), the results of which were announced on April 14, 2015. The auction was intended to procure adequate supplies through 2016 for most of downstate and midstate Illinois. The bidding strategies of Dynegy and other suppliers, combined with the rules under which the auction was conducted, pushed auction prices up for much of Illinois from \$16.75 per megawatt-day last year to \$150 this year, an increase of 800 percent. Even if illegal manipulation did not occur, the dramatic spike—resulting in a rate for Illinois that is more than 40 times that in neighboring states despite abundant generating capacity in Illinois—indicates a violation of the Federal Power Act's fundamental requirement that rates be just and reasonable. These are the sort of market abuses that impact small business and demand a regulatory response.

**Remedies:** New rules should be created to ensure transparency standards apply to the non-governmental agencies, known as Regional Transmission Organizations, charged with running deregulated electricity markets. New rules should be established to ensure consumer, small business and state government representation in their decision-making

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Responses to Abusive Patent Troll Enforcement Practices. Available from:

<[http://www.antitrustinstitute.org/~antitrust/sites/default/files/PAE%20Workshop%20\(3051321\\_1\).pdf](http://www.antitrustinstitute.org/~antitrust/sites/default/files/PAE%20Workshop%20(3051321_1).pdf)>.

<sup>155</sup> Moss, D. (2013, Jan. 10.) *Collusive Agreements in the Energy Industry: Insights into U.S. Antitrust Enforcement*. American Antitrust Institute. p. 6. Available from:

<[http://www.antitrustinstitute.org/~antitrust/sites/default/files/AAI%20Working%20Paper%2013-2\\_%20Section%201%20Energy.pdf](http://www.antitrustinstitute.org/~antitrust/sites/default/files/AAI%20Working%20Paper%2013-2_%20Section%201%20Energy.pdf)>.

<sup>156</sup> Public Citizen, Inc. v. Midcontinent Independent System Operator, Inc.. Emergency Section 206 Complaint of Public Citizen, Inc. And Request For Fast Track Processing, May 28, 2015, Available from: <<http://www.citizen.org/pressroom/pressroomredirect.cfm?ID=5533>>.

processes. Additionally, legislation or perhaps new regulation is needed to overturn the "filed rate doctrine," which can immunize electricity traders from antitrust liability where conduct involves regulated, filed rates.

- Private antitrust enforcement—an important tool for small firms victimized by unfair practices from larger competitors—has become increasingly difficult. One notable obstacle to effective private enforcement are unreasonably high pleading standards, which require victimized plaintiffs to make evidentiary showings that they frequently cannot make before undertaking discovery.

**Remedies:** Congress should act to overturn the ruling in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), as well as *Ashcroft v. Iqbal*, 556 U.S. 662 (2009).

- Forced arbitration provisions in contracts are denying small businesses and consumers effective access to justice on a large scale. These provisions also often unfairly treat small business franchisees, which are often victimized by forced arbitration provisions in their franchise agreements.

In recent years, the Supreme Court has issued a series of rulings holding that the pro-arbitration preference of the Federal Arbitration Act preempts state rules designed to ensure consumers access to traditional civil courts, as well as state rules protecting consumers' rights to join together in class actions. As a result, large corporations are able to include forced arbitration provisions in standard form contracts; and to insert anti-class action language into their arbitration provisions as a way to block collective actions that are often critical to addressing wrongdoing that affects large numbers of people in a small way.

The Supreme Court's 2013 decision in *American Express v. Italian Colors Restaurant* illustrates the potential stakes for small business.<sup>157</sup> In this case, American Express sought to enforce an arbitration agreement that prohibits merchants that accept its charge cards from filing class actions or otherwise sharing the cost of legal proceedings against it. The merchants aimed to hold American Express liable for a tying arrangement that allegedly violated antitrust laws (American Express insists merchants accept its unpopular credit cards if they want to accept its popular charge cards), but because expensive expert testimony was required to prove the claims, the cost of arbitrating an individual case would dwarf any possible recovery. Even in this case, where the arbitration agreement and class action ban concededly made it impossible for a small business to bring an antitrust lawsuit against a large company, the Supreme Court held that the arbitration agreement was controlling. It did not matter to the Court that this was a case where a large company used its market power to force on small business a provision that prevents them from seeking a remedy to an abuse of market power.

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<sup>157</sup> *American Express v. Italian Colors Restaurant*, 570 U. S. \_\_\_\_ (2013).



**Remedies:** Congressional remedies to these problems should include a prohibition on forced arbitration provisions in consumer, employment and civil rights cases<sup>158</sup> and a restoration of states' authority to enforce their contract and consumer protection laws.

### **III. Conclusion: Strengthening the System of Regulatory Protections to Strengthen America**

There is much to celebrate in our nation's system of regulatory protections. It has tamed marketplace abuses and advanced the values we hold most dear: freedom, safety, security, justice, competition and sustainability. We should celebrate the achievements of regulatory protections.

But in its current form, the regulatory system is failing to meet its promise. Rather than looking at how to scale back or hinder the regulatory system, Congress should look to reforms to strengthen regulatory enforcement, stiffen penalties for corporate wrongdoing, speed the rulemaking process, address uneven judicial review of regulations, and adopt pro-competitive rules to level the playing field for small business and improve the economy and consumer well-being.

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<sup>158</sup> See the Arbitration Fairness Act, S. 1133, introduced by Senator Al Franken.



**THE LABOR DEPARTMENT'S FIDUCIARY RULE: HOW A  
FLAWED PROCESS COULD HURT RETIREMENT SAVERS**

A Majority Staff Report of the  
Committee on Homeland Security and Governmental Affairs  
United States Senate  
Senator Ron Johnson, Chairman



February 24, 2016

## EXECUTIVE SUMMARY

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For millions of Americans, retirement saving is an important step in ensuring a comfortable standard of living well past employment. However, the process of saving for retirement can be difficult, confusing, and scary. To navigate the wide array of saving plans and options, individuals often turn to investment advisors for advice. A 2015 study reported that receiving investment advice significantly increases retirement savings.<sup>1</sup> According to the report, among individuals with \$100,000 or less in annual income, individuals who receive investment advice save at least 38% more than individuals who do not receive investment advice.<sup>2</sup> For individuals of retirement age (65 and older), the disparity increases: advised individuals have more than double the assets of non-advised individuals.<sup>3</sup>

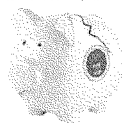
The Department of Labor issued a proposed rule (“rule,” “proposed rule,” or “proposal”) on April 20, 2015, which would expand the definition of a fiduciary under the Employee Retirement Income Security Act of 1974 (ERISA). The Labor Department’s proposed rule redefined the term “investment advice” to encompass activities that occur within pension and retirement plans, but that do not constitute investment advice under the existing definition of investment advice. The Labor Department touts its rule as a necessary reform to the investment advice industry to ensure that investment advisors avoid conflicts of interest and act in the best interest of their clients.

In February 2015, Senator Ron Johnson, Chairman of the Senate Committee on Homeland Security and Governmental Affairs, initiated an inquiry to examine the Labor Department’s fiduciary rulemaking. This inquiry found that career, non-partisan professional staff at the Securities and Exchange Commission (SEC); regulatory experts at the Office of Information and Regulatory Affairs (OIRA) within the Office of Management and Budget (OMB); and Treasury Department officials expressed numerous concerns to the Labor Department about its proposed rule. Documents obtained by the Committee also indicate that officials at the Labor Department disregarded many of these concerns and declined to implement recommendations from the SEC, OIRA, and the Treasury Department. The majority staff found that the Labor Department frequently prioritized the expeditious completion of the rulemaking process at the expense of thoughtful deliberation. Additionally, the majority staff found indications that political appointees at the White House played a key role in driving the rulemaking process at the inception of the redrafting effort.

<sup>1</sup> OLIVER WYMAN, THE ROLE OF FINANCIAL ADVISORS IN THE US RETIREMENT MARKET 16 (2015)

<sup>2</sup> *Id.*; *Restricting Advice and Education: DOL’s Unworkable Investment Proposal for American Families and Retirees*, Hearing Before the Subcomm. on Emp’t & Workplace Safety of the S. Comm. on Health, Educ., Labor & Pensions, 114th Cong. (2015) [hereinafter Senate HELP Committee Hearing] (statement of Peter Schneider, President, Primerica, Inc.).

<sup>3</sup> WYMAN, *supra* note 1; Senate HELP Committee Hearing (statement of Peter Schneider), *supra* note 2.



**Majority Staff Report**  
**Committee on Homeland Security and Governmental Affairs**  
**United States Senate**

Specifically, the report's findings include the following information:

- Despite public assurances that the Labor Department had collaborated with the SEC, emails between a Labor Department employee and an SEC expert reveal discord between the agencies about the rulemaking. The Labor Department employee wrote to his SEC counterpart: "Well, I hate to break it to you, but you're wrong," and **"We have now gone far beyond the point where your input was helpful to me. . . . If you have nothing new to bring up, please stop emailing me."** The SEC staffer responded: **"I am now also utterly confused as to what the purpose of the proposed DOL rule is . . ."**<sup>4</sup>
- Career, non-partisan SEC staff identified at least 26 items of concern related to the substantive content of the proposed rule, and the Labor Department declined to fully resolve all of the concerns.<sup>5</sup>
- After the Labor Department sought to address to the SEC's stated items of concern, a senior SEC official emphasized to the Labor Department that concerns remained:  
*[W]e continue to believe that commentators are likely to raise concerns that the proposal may result in reduced pricing options, rising costs and limited access to retirement advice, particularly for retail investors. Commentators also may express concerns that broker-dealers, as a practical matter, may be unlikely to use the exemptions provided and may stop providing services because of the number of conditions imposed, likely compliance costs, and lack of clarity around several provisions.*<sup>6</sup>
- The Labor Department rejected the SEC's recommendation and ignored the requirements of Executive Orders 12866 and 13563 to quantify the costs and benefits of alternative approaches. As a Labor Department employee explained, **"We think this would be extraordinarily difficult and would appreciably delay the project for very little return . . ."**<sup>7</sup>
- Treasury officials voiced concerns that the Labor Department's proposal, by attempting to regulate IRAs through the proposed rule, "fl[ies] in the face of logic" and was contrary to Congressional intent. The Labor Department promulgated the proposed rule less than two weeks after circulating this draft, undoubtedly limiting the extent to which the Department considered the comments it received from the Treasury Department.<sup>8</sup>
- The Administration was predetermined to regulate the industry and sought evidence to justify its preferred action. In emails to senior White House advisors, a Labor Department official wrote of the **"challenges in completing the [regulatory impact**

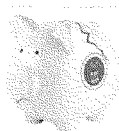
<sup>4</sup> *Infra* Part II(a).

<sup>5</sup> *Infra* Part II(a).

<sup>6</sup> *Infra* Part II(a).

<sup>7</sup> *Infra* Part II(a)(iv).

<sup>8</sup> *Infra* Part II(d).



analysis]” and of the need to find literature and data that “**can be woven together to demonstrate that there is a market failure and to monetize the potential benefits of fixing it.**” In another email, a Labor Department official discussed “**building the case for why the rule is necessary.**”<sup>9</sup>

- The Labor Department rejected OIRA’s recommendation to add language stating that the rule would “permit firms to continue *to rely on all* common fee and compensation practices . . . .” The Labor Department responded that “[n]ot all fee practices will be permitted by the exemptions” and that “[b]y deleting ‘all’ we slightly soften this by leaving it at ‘common fee and compensation practices.’”<sup>10</sup>

Investment advisors, in general, do not dispute the importance of acting in the best interest of their clients, and many advisors already abide by a best interest standard.<sup>11</sup> However, experts have criticized the proposed rule as burdensome and complex,<sup>12</sup> and have challenged the Labor Department’s claims that the rule will generate benefits for investors.<sup>13</sup> They contend that the Administration has reported inflated numbers for the harm that results from investors relying on “conflicted advice,”<sup>14</sup> with one expert opining “[y]ou don’t have to be an economist to recognize the Administration’s \$17 billion talking point significantly overestimates the costs, if any, to investors relying on the ‘conflicted advice’ of brokers.”<sup>15</sup> Experts also caution that the proposal’s conditions and requirements would create uncertainty for investment advisors and would increase compliance costs and litigation risks. They warn that the Labor Department’s analysis overstates the rule’s benefits and that the rule could actually result in net losses to retirement savers.<sup>16</sup> These experts emphasize that the rule would actually harm the investors it is supposed to protect; the rule would drive up the price of investment advice and would ultimately decrease the availability of advice for low- and middle-income investors.

A 2015 report estimates that the rule will cause a loss of retirement savings of \$68–80 billion per year, and will “jeopardize retirement readiness for 11.9 million IRA and retirement participants.”<sup>17</sup> Robert Litan, an economist and attorney who served as the associate director of

<sup>9</sup> *Infra* Part IV.

<sup>10</sup> *Infra* Part II(c).

<sup>11</sup> *E.g.*, Senate HELP Committee Hearing, *supra* note 2 (statement of Robert Litan).

<sup>12</sup> *Id.*

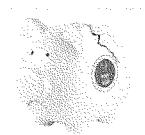
<sup>13</sup> *Id.* (statement of Peter Schneider); QUANTRIA STRATEGIES, LLC, UNINTENDED CONSEQUENCES: POTENTIAL OF THE DOL REGULATIONS TO REDUCE FINANCIAL ADVICE AND ERODE RETIREMENT READINESS 1 (2015) (prepared for Davis & Harman).

<sup>14</sup> EXEC. OFFICE OF THE PRESIDENT, THE EFFECTS OF CONFLICTED INVESTMENT ADVICE ON RETIREMENT SAVINGS (2015).

<sup>15</sup> Craig M. Lewis, *An Inflated \$17 Billion Talking Point From the DOL*, FORBES (Dec. 16, 2015, 12:30 PM), <http://www.forbes.com/sites/realspin/2015/12/16/an-inflated-17-billion-talking-point-from-the-dol/#782b028439e1>.

<sup>16</sup> QUANTRIA STRATEGIES, *supra* note 13, at 1; Senate HELP Committee Hearing, *supra* note 2 (statement of Robert Litan).

<sup>17</sup> QUANTRIA STRATEGIES, *supra* note 13, at 1; Senate HELP Committee Hearing, *supra* note 2 (statement of Peter Schneider).



the White House budget office in the Clinton Administration, predicts that seven million or more small investors could lose their brokers as a result of the rule.<sup>18</sup> This would be costly to investors, who may make worse investing decisions when they do not receive human investment advice.<sup>19</sup>

Some observers suggest that this is actually an *intended* effect of the rule, and that the Labor Department believes that low- and middle-income investors should receive advice primarily from robo-advisors to avoid conflicts of interest.<sup>20</sup> If accurate, it is alarming that the Labor Department is intentionally restricting low- and middle-income investors to robo-advice based on a presumption that those investors lack the sophistication to interact with an individual investment advisor and to understand options presented to them.

As the majority staff puts forward its findings, it is important to note that Chairman Johnson performed this oversight in the face of continuous obstruction from the Labor Department. In February 2015, Chairman Johnson requested documents, including communications between the Labor Department and the White House and between the Labor Department and the SEC. However, to date, the Labor Department has not fulfilled Chairman Johnson's requests. The Labor Department has produced no material responsive to Chairman Johnson request for communications between the Department and the White House. The Department initially claimed that no responsive documents existed, but refused to provide Chairman Johnson with information about how Labor Department officials searched for documents. Chairman Johnson later received, from the SEC, communications between the Department and the White House. Additionally, the Department has produced only a limited subset of self-selected communications between the Department and the SEC and provided short briefings to the Committee. These productions fall short of full compliance. Most egregiously, the Labor Department even urged the SEC to similarly hinder Chairman Johnson's oversight work by asking the SEC to reject the Chairman's separate requests to the SEC for documents in the control and possession of the SEC.

Due to the Labor Department's obstructionism, Chairman Johnson and the majority staff have not had the opportunity to review the full universe of documents and communications related to the rule. The analysis and findings in this report are based on the information received. However, the information that Chairman Johnson was able to obtain strongly suggests that the Labor Department engaged in a flawed rulemaking process to craft a rule that will hurt millions of American retirement savers.

<sup>18</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Robert Litan).

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*



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## I. INTRODUCTION

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On April 20, 2015, the Department of Labor issued a proposed rule to expand the definition of a fiduciary under the Employee Retirement Income Security Act of 1974 (ERISA).<sup>21</sup> The Labor Department's proposed rule redefined the term "investment advice" to encompass activities that occur within pension and retirement plans, but do not constitute investment advice under the existing definition of investment advice.<sup>22</sup> The Labor Department's promulgation of this rule was the culmination of a years-long effort by the Department's Employee Benefits Security Administration (EBSA).<sup>23</sup>

Even before the latest proposal was announced, stakeholders began raising concerns that the rule would adversely affect access to investment advice for low- and middle-income Americans.<sup>24</sup> Additional questions were raised about the close involvement of the White House in shaping the proposal.<sup>25</sup> In light of these concerns, Senator Ron Johnson, Chairman of the Senate Committee on Homeland Security and Governmental Affairs, initiated an inquiry in early February 2015.<sup>26</sup>

Under Senate rules and precedent, the Committee has legislative jurisdiction over intergovernmental relations and the regulatory process of the federal government. The Committee also has specific authority to examine "the efficiency and economy of all branches and functions of Government with particular references to the operations and management of Federal regulatory policies and programs."<sup>27</sup> Chairman Johnson initiated the inquiry pursuant to these authorities.

Chairman Johnson sought to examine the Labor Department's rulemaking process to ensure that the Department solicited and fully considered advice from career, non-partisan professionals with expertise in the proposal's subject matter.<sup>28</sup> As part of its inquiry, Chairman Johnson requested information and documents from the Securities and Exchange Commission

<sup>21</sup> CONG. RESEARCH SERV., R44207, DEPARTMENT OF LABOR'S 2015 PROPOSED FIDUCIARY RULE: BACKGROUND AND ISSUES 1 (2015).

<sup>22</sup> *Id.*

<sup>23</sup> Mark Schoeff, *DOL Proposal of Fiduciary-Duty Rule Delayed Again*, INVESTMENT NEWS (May 28, 2014, 8:30 AM), <http://www.investmentnews.com/article/20140528/FREE/140529932/dol-proposal-of-fiduciary-duty-rule-delayed-again>.

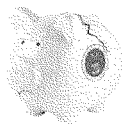
<sup>24</sup> *Id.*

<sup>25</sup> E.g., Melanie Waddell, *White House Getting Involved with DOL Fiduciary Redraft*, THINK ADVISOR (July 1, 2014), <http://www.thinkadvisor.com/2014/07/01/white-house-getting-involved-with-dol-fiduciary-re>.

<sup>26</sup> Appendix A, Ex. 1, Letter from Hon. Ron Johnson, Chairman, S. Comm. on Homeland Sec. & Governmental Affairs (HSGAC), to Hon. Thomas E. Perez, Sec'y, U.S Dep't of Labor (DOL) (Feb. 5, 2015).

<sup>27</sup> S. Res. 73 § 12, 114th Cong. (2015).

<sup>28</sup> See Appendix A, Ex. 1, Letter from Chairman Johnson to Sec'y Perez, DOL (Feb. 5, 2015); Appendix A, Ex. 2, Letter from Chairman Johnson to Sec'y Perez, DOL (Mar. 17, 2015).



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(SEC),<sup>29</sup> the Financial Industry Regulatory Authority (FINRA),<sup>30</sup> the Office of Information and Regulatory Affairs (OIRA),<sup>31</sup> the Department of the Treasury,<sup>32</sup> and the Labor Department.<sup>33</sup> In response, the SEC provided three document productions to the Committee.<sup>34</sup> These productions, which the SEC made despite the Labor Department's attempt to persuade the SEC to reject the Chairman's requests,<sup>35</sup> shed significant light on the recommendations and concerns that career, non-partisan, professional staff at the SEC provided prior to the release of the proposal. The SEC documents also shed light on aspects of the recommendations and concerns offered by regulatory experts at OIRA and from Treasury Department officials. FINRA additionally provided two document productions to the Committee.<sup>36</sup> OIRA provided one document production, although it was largely nonresponsive to Chairman Johnson's requests.<sup>37</sup> Finally, the Committee received a limited subset of documents from the Labor Department regarding its communications with the SEC; however, the Labor Department continues to withhold other responsive documents from the Committee.<sup>38</sup>

Based on the information received by the Committee, the majority staff has found that career, non-partisan, professional staff at the SEC, regulatory experts at OIRA, and Treasury Department officials expressed concerns to the Labor Department about its proposed rule. While Chairman Johnson and the majority staff do not have access to the entirety of Labor Department records, it appears that the Labor Department ignored and rejected many concerns and recommendations by subject-matter and regulatory experts.

<sup>29</sup> Appendix A, Ex. 3, Letter from Chairman Johnson to Hon. Mary Jo White, Chair, SEC (Apr. 21, 2015); Appendix A, Ex. 4, Letter from Chairman Johnson to Chairwoman White, SEC (May 20, 2015); Appendix A, Ex. 5, Letter from Chairman Johnson to Chairwoman White, SEC (July 13, 2015).

<sup>30</sup> Appendix A, Ex. 6, Letter from Chairman Johnson to Richard Ketchum, Chairman, FINRA (Sept. 16, 2015).

<sup>31</sup> Appendix A, Ex. 7, Letter from Chairman Johnson to Hon. Howard Shelanski, Admin'r, OIRA (May 1, 2015);

Appendix A, Ex. 8, Letter from Chairman Johnson to Admin'r Shelanski, OIRA (Dec. 3, 2015).

<sup>32</sup> Appendix A, Ex. 9, Letter from Chairman Johnson to Hon. Jacob Lew, Sec'y, Treasury Dep't (Nov. 12, 2015).

<sup>33</sup> Appendix A, Ex. 3, Letter from Chairman Johnson to Chairwoman White, SEC (Apr. 21, 2015).

<sup>34</sup> Appendix A, Ex. 10, Letter from Chairwoman White, SEC, to Chairman Johnson (May 5, 2015); Appendix A, Ex. 11, Letter from Tim Henseler, Dir., Office of Leg. & Intergovernmental Affairs, SEC, to Chairman Johnson (July 27, 2015); Appendix A, Ex. 12, Letter from Tim Henseler, SEC, to Chairman Johnson (Sept. 15, 2015); Appendix A, Ex. 13, Letter from Tim Henseler, SEC, to Chairman Johnson (Nov. 25, 2015) (complete document productions on file with Committee).

<sup>35</sup> Appendix A, Ex. 14, Letter from Adri Jayaratne, Acting Asst. Sec'y, Office of Cong. & Intergovernmental Affairs, DOL, to Chairman Johnson (July 8, 2015).

<sup>36</sup> Appendix A, Ex. 15, Letter from Robert Colby, Exec. VP & Chief Legal Officer, FINRA, to Chairman Johnson (Oct. 15, 2015); Appendix A, Ex. 16, Letter from Robert Colby, FINRA, to Chairman Johnson (Oct. 29, 2015).

<sup>37</sup> Appendix A, Ex. 17, Letter from Admin'r Shelanski, OIRA, to Chairman Johnson (May 18, 2015); Appendix A, Ex. 18, Letter from Admin'r Shelanski, OIRA, to Chairman Johnson (Jan. 20, 2016).

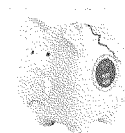
<sup>38</sup> Appendix A, Ex. 19, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (Feb. 9, 2015);

Appendix A, Ex. 20, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (Feb. 23, 2015); Appendix A, Ex. 21, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (Mar. 23, 2015);

Appendix A, Ex. 22, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (Apr. 3, 2015);

Appendix A, Ex. 23, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (June 15, 2015);

Appendix A, Ex. 14, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (July 8, 2015); Appendix A, Ex. 24, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (July 27, 2015).



The Department's proposal appears to be a solution in search of a problem, driven by ideology rather than a market need. As a result, some studies suggest that the proposal could result in losses to retirement savers of \$68–80 billion each year and will drive smaller investment advisors out of the marketplace.<sup>39</sup> Experts have criticized the Labor Department's rule as burdensome and complex and caution that the rule's conditions and requirements will create uncertainty for investment advisors and drive up compliance costs and litigation risks.<sup>40</sup> Ultimately, the rule will likely prompt investment advisors to increase the price of services they offer to investors and to reduce the services they provide to middle-income investors.<sup>41</sup>

## II. THE LABOR DEPARTMENT DECLINED TO INCORPORATE RECOMMENDATIONS FROM SUBJECT-MATTER AND REGULATORY EXPERTS

### a. The Labor Department Declined to Incorporate Recommendations from Career Experts at the SEC into the Proposed Rule

Under the Dodd-Frank Act, the SEC has authority to regulate standards of care for broker-dealers and investment advisers.<sup>42</sup> Section 913 of the Dodd-Frank Act directed the SEC to examine existing regulations, evaluate their potential effects on retail customers, and to recommend fiduciary standards to govern the industry.<sup>43</sup> Additionally, based on the authority granted by the Investment Advisers Acts in 1940, the SEC has historically regulated the investment industry.<sup>44</sup> The SEC is, therefore, the proper entity with the appropriate securities law expertise, to consider issues such as requiring a best interest standard for investment advisors. The SEC has reported plans to issue a uniform regulation governing retail investment advice, which could result in "two incredibly burdensome and redundant rules"<sup>45</sup> disseminated by the Labor Department and the SEC.<sup>46</sup>

<sup>39</sup> QUANTRIA STRATEGIES, *supra* note 13, at 1.

<sup>40</sup> *Infra* Part III.

<sup>41</sup> *Infra* Part III.

<sup>42</sup> The Dodd-Frank Wall Street Reform and Consumer Protection Act § 913, 124 Stat. 1376 (2010).

<sup>43</sup> *Id.*; MEGAN MILLOY, AM. ACTION FORUM, DOL'S PROPOSED FIDUCIARY RULE: NOT IN THE BEST INTEREST OF INVESTORS (2015).

<sup>44</sup> Investment Advisers Act of 1940, 15 U.S.C. § 80b-1.

<sup>45</sup> Appendix A, Ex. 25, Letter from Daniel Gallagher, Comm'r, SEC, to Sec'y Perez, DOL (July 21, 2015).

<sup>46</sup> SEC Office of Mgmt. & Budget Fall Agenda, Personalized Investment Advice Standard of Conduct, *available at* <http://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201510&RIN=3235-AL27> (scheduling a notice of proposed rulemaking for October 2016); Mark Schoeff, Jr., *SEC's Mary Jo White Says Agency Will Develop Fiduciary Rule for Brokers*, INVESTMENT NEWS (Mar. 17, 2015, 12:31 PM), <http://www.investmentnews.com/article/20150317/FREE/150319919/secs-mary-jo-white-says-agency-will-develop-fiduciary-rule-for>.



The Labor Department has authority under ERISA to regulate private-sector, employer-provided benefit plans. However, according to the former head of EBSA, the Labor Department has significantly departed from its traditional view of its jurisdiction by attempting to regulate compensation and conduct for *all* types of financial advisors, including registered investment advisors and registered representatives of broker dealers.<sup>47</sup> At a minimum, given the SEC staff's expertise in securities regulation and the potential for conflict between the two rules, the Labor Department should have ensured that its rule incorporated recommendations and addressed concerns voiced by professional experts at the SEC.

However, former SEC Commissioner Daniel Gallagher emphasized that the Labor Department did not collaborate with the SEC in the rulemaking process.<sup>48</sup> Commissioner Gallagher called the rulemaking a “fait accompli” and criticized the comment process for being “merely perfunctory.”<sup>49</sup> Commissioner Gallagher dispelled Department of Labor Secretary Thomas Perez’s claims that the Labor Department “met substantively” with career, non-partisan staff at the SEC, pointing out that Commissioner Gallagher was not included in any such conversations.<sup>50</sup> Commissioner Gallagher wrote that, in contrast to Secretary Perez’s claims, “the [Labor Department’s] actions, and the substance of the [Labor Department] Fiduciary Proposal, reflect a lack of concern for the [SEC’s] views on these issues.”<sup>51</sup> He continued:

Strikingly, the Fiduciary Proposal does not contemplate or even mention potential SEC rules or the SEC’s existing regime for regulating broker-dealers and investment advisers. If the DOL were actually serious about working together with the SEC on an implementable standard, it could have—and should have—included in its proposal some type of substituted compliance mechanism, in which compliance with an SEC fiduciary standard would satisfy the DOL rules.<sup>52</sup>

Chairman Johnson has obtained information that supports Commissioner Gallagher’s position that the Labor Department failed to work in good faith with the career, non-partisan, professional staff at the SEC. For more than a year preceding the Labor Department’s promulgation of the proposed rule, SEC staff received draft portions of the proposed rulemaking package, including a draft regulatory impact analysis, draft global exemption (Best Interest Contract Exemption), and background on the point of sale disclosure.<sup>53</sup> Communications between the Labor Department and the SEC staff reveal numerous instances in which the Labor Department requested advice from SEC staff on fundamental aspects of the proposal, but

<sup>47</sup> *Hearing on the Department of Labor’s Proposed Fiduciary Rule Before the Subcomm. on Oversight of the H. Comm. on Ways & Means*, 114th Cong. (2015) [hereinafter House Ways & Means Committee Hearing] (statement of Bradford Campbell).

<sup>48</sup> Appendix A, Ex. 25, Letter from Comm’r Gallagher, SEC to Sec’y Perez, DOL (July 21, 2015).

<sup>49</sup> *Id.*

<sup>50</sup> *Id.*

<sup>51</sup> *Id.*

<sup>52</sup> *Id.*

<sup>53</sup> Briefing by Staff, DOL, to Committee Staff, HSGAC (Aug. 28, 2015) (notes on file with Committee).



disagreed with the SEC's recommendations and, in doing so, disregarded the SEC staff's subject-matter expertise.

Although Secretary Perez publicly assured stakeholders that the Labor Department collaborated with the SEC and “worked extensively with colleagues throughout the government, including and especially the [SEC],”<sup>54</sup> documents obtained by the Committee paint another picture. A series of emails in July and August 2012 reveal disagreements between Labor Department staff and SEC staff about the type of improper activity the proposal should measure. The SEC staff suggested that the proposal should measure conflicts of interest, whereas the Labor Department sought to measure investment returns.<sup>55</sup> These men were apparently classmates in a PhD program—which may account for the candid tone of the emails—but the email exchange suggests that the Labor Department disregarded an SEC expert's serious concerns about the rule.<sup>56</sup> In one email, after a lengthy discussion of the proposal, a Labor Department staffer wrote to an SEC staffer:<sup>57</sup>

<sup>54</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Thomas Perez, Sec'y of Labor).

<sup>55</sup> Appendix B, Ex. 1, Emails between Matthew Kozora, SEC, and Keith Bergstresser, U.S. Dep't of Labor (July 2012), SEC-DOL008040-008052.

<sup>56</sup> The Labor Department represented to Committee staff that the Labor Department employee, Keith Bergstresser, and the SEC employee, Matthew L. Kozora, attended school together. Mr. Bergstresser received a Ph.D. in Economics from the University of Maryland, College Park, in 2009, and has been an economist at the Labor Department since June 2009. See LinkedIn.com, Keith Bergstresser, <https://www.linkedin.com/in/keith-bergstresser-10651482>. He serves in the Office of Policy and Research within the Employee Benefits and Security Administration. *In re: Conflict of Interest Proposed Rule, Related Exemptions, and Regulatory Impact Analysis Hearing*, U.S. Dep't of Labor, Employee Benefits Security Admin. (Aug. 11, 2015). Mr. Bergstresser reports to the head of EBSA, Assistant Secretary Phyllis Borzi, a presidentially appointed official who has been described as the “main architect” of the fiduciary rule. Melanie Waddell, *DOL to ‘Simplify and Streamline’ Fiduciary Rule: Borzi*, THINKADVISOR (Oct. 20, 2015). Mr. Kozora received a Ph.D. in Finance from the University of Maryland, College Park, in 2010, and has been a financial economist at the SEC since 2010. See Matthew L. Kozora, Financial Economist, Office of Asset Management, SEC.gov, <http://www.sec.gov/divisions/riskfin/economistbios/matthew-l-kozora.shtml>. Mr. Kozora serves in the Office of Asset Management within the Division of Economic and Risk Analysis. *Id.* As the SEC's “think tank,” the Division provides “detailed, high-quality economic and statistical analyses, and specific subject-matter expertise . . .” *About the Division of Economic and Risk Analysis*, SEC.GOV, <https://www.sec.gov/dera/about>. Ultimately, the SEC's regulatory authority is vested in a bipartisan, five-member commission who serve staggered terms—in the words of the SEC, “ensuring non-partisanship.” *The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, SEC.GOV, <https://www.sec.gov/about/whatwedo.shtml>. While both men possess financial expertise, the different structures of their respective agencies and the Labor Department's advocacy for the rulemaking appear to have caused the men to adopt differing opinions about the Labor Department's proposal.

<sup>57</sup> Appendix B, Ex. 1, Email from Keith Bergstresser, U.S. Dep't of Labor, to Matthew Kozora, SEC (July 31, 2012, 1:49 PM), SEC-DOL008057-008058.



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**From:** Bergstresser, Keith - EBSA [REDACTED]@dol.gov]  
**Sent:** Tuesday, July 31, 2012 1:50 PM  
**To:** Kozora, Matthew  
**Subject:** RE: question

Well, I hate to break it to you, but you're wrong. People do not respond to fees or any other costs, but they do chase returns. This and our other reasons for choosing the disclosure that we have developed are laid out in the document that we've already sent over to you (attached). You might try reading the paragraph labeled "Portfolio Returns" on page 4. And do look into the references. They are very convincing.

In a later email, Labor Department staff dismissively wrote to the SEC financial economist:<sup>58</sup>

**From:** Bergstresser, Keith - EBSA [REDACTED]@dol.gov]  
**Sent:** Tuesday, July 31, 2012 3:23 PM  
**To:** Kozora, Matthew  
**Subject:** RE: question

See my responses below. We have now gone far beyond the point where your input was helpful to me. You keep circling back to the same statements, many of which are unsupported conjectures on your part, and most of which I have addressed even before you brought them up. Yet, your statements do not seem to even acknowledge the points that I already made (with supporting evidence) in the document we sent. If you have nothing new to bring up, please stop emailing me about this topic.

<sup>58</sup> Appendix B, Ex. 1, Email from Keith Bergstresser, U.S. Dep't of Labor, to Matthew Kozora, SEC (July 31, 2012, 3:22 PM), SEC-DOL008056.



The SEC financial economist responded, expressing confusion about the fundamental purpose of the Labor Department's proposal.<sup>59</sup>

**From:** Kozora, Matthew [REDACTED]@SEC.GOV  
**Sent:** Tuesday, July 31, 2012 3:43 PM  
**To:** Bergstresser, Keith - EBSA  
**Subject:** RE: question

I apologize if I have overstepped my boundaries. This is a difficult topic for sure, and I was under the impression that my opinion was a. helpful and b. wanted.

I am also now utterly confused as to what the purpose of the proposed DOL rule is then, if not to limit advisor conflicts when providing retirement advice? Considering that my prior is that the DOL wants to reduce advisor conflicts, it just seems logical to me that the end result should measure advisory conflicts.

Good luck with your rulemaking.

Matt

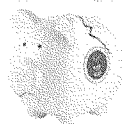
Finally, SEC staff expressed concern about "intent of the measure itself," and wrote that the SEC and the Labor Department "just have two opposing viewpoints on the matter."<sup>60</sup> Labor Department staff deferred continuing the conversation to a later date,<sup>61</sup> but documents the Committee received provide no indication of future discussion on this topic. The SEC staff also raised concerns about the Labor Department's reliance on psychology literature to draft the rule, which would result in comparisons that "have very little economic meaning and thus no value to consumers."<sup>62</sup>

<sup>59</sup> Appendix B, Ex. 1, Email from Matthew Kozora, SEC, to Keith Bergstresser, U.S. Dep't of Labor (July 31, 2012, 3:42 PM), SEC-DOL008055-008056.

<sup>60</sup> Appendix B, Ex. 1, Email from Matthew Kozora, SEC, to Keith Bergstresser, U.S. Dep't of Labor (Aug. 2, 2012, 11:57 AM), SEC-DOL008054-008055.

<sup>61</sup> Appendix B, Ex. 1, Email from Keith Bergstresser, U.S. Dep't of Labor, to Matthew Kozora, SEC (Aug. 2, 2012, 2:00 PM), SEC-DOL008054.

<sup>62</sup> Appendix B, Ex. 1, Email from Matthew Kozora, SEC, to Keith Bergstresser, U.S. Dep't of Labor (Aug. 2, 2012, 11:57 AM), SEC-DOL008054-008055.



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**From:** Bergstresser, Keith - EBSA [REDACTED]@dol.gov]  
**Sent:** Tuesday, July 31, 2012 4:15 PM  
**To:** Kozora, Matthew  
**Subject:** RE: question

I would be happy to have a phone conversation to discuss the purpose of the rule, the purpose of the exemption conditions and distinctions between the two. don't think I want to try to have that conversation via email. I might have some time tomorrow, but I'm at a conference Thursday and Friday and then on vacation next week.

**From:** Kozora, Matthew [REDACTED]@SEC.GOV]  
**Sent:** Thursday, August 02, 2012 11:57 AM  
**To:** Bergstresser, Keith - EBSA  
**Subject:** RE: question

Dear Keith,

There is a fundamental difference between price variation and the risk investors bear. For instance, prices may not change over a given period of time but yet investors might still bear much risk. There will also be problems with respect to measuring price variation with respect to illiquid securities or securities that are not traded very often (muni bonds, structured products, real estate). You are also treating systematic risk with idiosyncratic risk equally. Literature tells us (Sharpe (1964), Lintner (1965)) that such risks are not the same and should be treated much differently.

I understand you want to measure returns due to the psychology literature, however, I am quite concerned your benchmarks based on ex-post price variation will make such comparisons have very little economic meaning and thus no value to consumers. I am also concerned as to the intent of the measure itself. Do you want to "weed out" bad providers of advice by reporting performance measures? Or do you want to "protect participants from conflicts of interest" as proposed rule suggests? Those are two separate and different intents.

If/when you have a formal rule proposal that you want comments on, I will be more than happy to share my thoughts and views. Otherwise, I think we just have two opposing viewpoints on the matter.

Matt



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It is evident from these emails that the SEC's expert staff had serious concerns about the rule. The financial economist at the SEC emailed Labor Department staff repeatedly and expressed serious concerns about fundamental principles of the rule. However, not only did the Labor Department dismiss the concerns, but the Department went a step further by actually demanding that the SEC expert stop emailing about the proposal.

The Labor Department restricted the Committee's review of these emails to a limited *in camera* review.<sup>63</sup> The Committee, however, ultimately obtained the communications from another source.

The SEC received the full proposed rulemaking package from the Labor Department in November 2014 and exchanged edits and comments with the Labor Department in January 2015.<sup>64</sup> Career, non-partisan SEC staff identified at least 26 items of concern related to the substantive content of the proposed rule.<sup>65</sup> The SEC staff's concerns included issues of clarity in the rule's "best interest" standard, inadvertent consequences of a *de minimis* breach, conflicts with federal securities laws and FINRA rules, and a lack of cost-benefit analysis of alternatives.<sup>66</sup> The SEC's point of contact in transmitting these concerns to the Labor Department was Sharon Block, a Senior Counselor to the Secretary of Labor, who formerly served as a political advisor in the Obama Administration, and whom President Obama recess appointed to be a member of the National Labor Relations Board, an appointment ultimately struck down by the Supreme Court.<sup>67</sup> The Labor Department repeatedly provided an incomplete response, declined to accept the SEC staff's recommendations, or incorrectly implemented the SEC expert's recommendations.<sup>68</sup> Specifically, in response to eight recommendations, the Labor Department declined to edit the operative language of the proposal, and instead merely modified or added language in the proposal's preamble.<sup>69</sup> The Labor Department outright rejected the SEC's two recommendations related to providing a quantitative cost-benefit analysis of considered alternatives to the rule.<sup>70</sup> Finally, the Labor Department implemented incorrect or

<sup>63</sup> The Department of Labor provided Committee staff with an *in camera* review of a limited subset of self-selected documents on August 28, 2015. Notes are on file with the Committee.

<sup>64</sup> See Appendix B, Ex. 2, E-mail from Lona Nallengara, SEC, to Sharon Block, DOL (Jan. 26, 2015, 7:36 PM), SEC-DOL003234-003239 [hereinafter Items of Concern Chart] (attachment is a chart containing items of concern about the proposed rule).

<sup>65</sup> *Id.*

<sup>66</sup> *Id.*

<sup>67</sup> Edward-Isaac Dove, *White House Pulls Controversial NLRB Pick*, POLITICO (Nov. 12, 2014), <http://www.politico.com/story/2014/11/nlr-sharon-block-lauren-mcferran-112833>; Melanie Trotman, *President Obama Taps Former NLRB Recess Appointee for Board Again*, WSJ (July 11, 2014, 3:34 PM), <http://www.wsj.com/articles/president-obama-taps-former-nlr-recess-appointee-for-board-again-1405101028>.

<sup>68</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239.

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*



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insufficient edits in response to at least four of the SEC's recommendations, evidenced by the SEC staff's follow-up on multiple issues of concern.<sup>71</sup>

Following the SEC staff's exchange of recommendations and concerns with the Labor Department, SEC experts continued to raise concerns "regarding the complexity of the proposal," and noted that the Labor Department had not fully addressed the SEC staff's enumerated issues of concern.<sup>72</sup> Then-SEC Chief of Staff Lona Nallengara, who has 20 years of experience in capital markets and corporate finance law,<sup>73</sup> explained in a January 26, 2015 email to Ms. Block:<sup>74</sup>

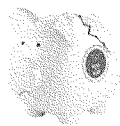
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<sup>71</sup> Appendix B, Ex. 3, Email from Lona Nallengara, SEC, to Sharon Block, DOL (Jan. 26, 2015), SEC-DOL003274-003276.

<sup>72</sup> *Id.*

<sup>73</sup> Press Release, SEC, SEC Chief of Staff Lona Nallengara to Leave Agency (May 19, 2015).

<sup>74</sup> Appendix B, Ex. 3, Email from Lona Nallengara, SEC, to Sharon Block, DOL (Jan. 26, 2015), SEC-DOL003274-003276.



**To:** Nallengara, Lona [REDACTED]@SEC.GOV]  
**Cc:** Hauser, Timothy - EBSA [REDACTED]@dol.gov; Porter, Jennifer R. [REDACTED]@SEC.GOV]  
**From:** Block, Sharon I - OSEC  
**Sent:** Mon 1/26/2015 7:40:58 PM  
**Importance:** Normal  
**Subject:** RE: EBSA responses to SEC comments

Thanks Lona. We appreciate all the time your team has put in and their thoughtful comments.

**From:** Nallengara, Lona [REDACTED]@SEC.GOV]  
**Sent:** Monday, January 26, 2015 7:37 PM  
**To:** Block, Sharon I - OSEC  
**Cc:** Hauser, Timothy - EBSA; Porter, Jennifer R.  
**Subject:** RE: EBSA responses to SEC comments

Sharon,

Thank you for sending the chart showing your responses to SEC staff comments on the rule package that we discussed with you in December.

We asked the staff to review the chart and below are a few additional thoughts from the staff on several of the items that you can consider as you prepare your proposal (the staff has identified their comments using the item numbers in your chart).

I would also like to note that although the chart shows that several changes were made to the proposal to address the potential concerns that we have discussed regarding the complexity of the proposal, we continue to believe that commenters are likely to raise concerns that the proposal may result in reduced pricing options, rising costs and limited access to retirement advice, particularly for retail investors. Commenters also may express concerns that broker-dealers, as a practical matter, may be unlikely to use the exemptions provided and may stop providing services because of the number of conditions imposed, likely compliance costs, and lack of clarity around several provisions.

We hope these comments will continue to be helpful to you as you finalize the proposed rules.

- Lona

Documents received by the Committee and language in the promulgated proposed rule indicate that the Labor Department declined to resolve these outstanding concerns.



**Majority Staff Report  
 Committee on Homeland Security and Governmental Affairs  
 United States Senate**

*i. The “Best Interest” Standard*

SEC staff recommended that the Labor Department add language to clarify the meaning of the term “best interest” in the proposal.<sup>75</sup> The Labor Department disregarded the recommendation, and stated that they “would prefer to see what commenters say before adding any additional explanatory language.”<sup>76</sup>

Indeed, commentators criticized the “best interest standard” in the promulgated proposal and recommended that the Labor Department clarify the standard’s requirements.<sup>77</sup> FINRA, the self-regulatory organization for the securities industry, focused on language requiring an investment advisor to provide advice that is in the best interest of the investor, “*without regard to the financial or other interests*” of the investment advisor.<sup>78</sup> FINRA explained that the “without regard to” phrase does not provide clear guidelines on limitations on compensation that varies depending on investment advice.<sup>79</sup>

Additionally, FINRA criticized the “best interest” standard’s requirement that financial institutions and advisors act prudently, explaining that the “prudence standard” could be “interpreted to require the financial institution and adviser to provide ongoing advice to the customer.”<sup>80</sup> FINRA recommended that the Labor Department make clear that the best interest standard does not require ongoing monitoring, and that the terms of the contract should control whether the financial institution or advisor will provide ongoing monitoring.<sup>81</sup>

Finally, FINRA questioned whether the Labor Department intended the best interest standard to require an investment advisor “to recommend the investment that is ‘best’ for the customer.”<sup>82</sup> FINRA reasoned that the Labor Department did intend such a result, and pointed to a statement by Secretary Perez, in which he stated:

If you’re an adviser operating under a suitability standard, once you narrow the options down to those that are suitable, you can recommend the one that is most lucrative for you—even though that might mean a lower return for the client. Under a best interest standard, you would need to choose the one that is the best for the client.<sup>83</sup>

<sup>75</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234–003239.

<sup>76</sup> *Id.*

<sup>77</sup> Appendix A, Ex. 26, Letter from Marcia E. Asquith, Sr. Vice President & Corp. Sec’y, FINRA, to DOL, at 6–8 (July 17, 2015) [hereinafter FINRA Comments].

<sup>78</sup> *Id.* at 6 (emphasis added).

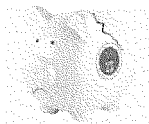
<sup>79</sup> *Id.*

<sup>80</sup> *Id.* at 7.

<sup>81</sup> *Id.* at 8.

<sup>82</sup> *Id.* at 7.

<sup>83</sup> *Id.*



FINRA cautioned that such a standard “would impose unnecessary and untenable litigation risks on fiduciaries,” and explained that reasonable investment advisors may consider different factors in evaluating products and may reach different conclusions about which product is the “best” product for the customer.<sup>84</sup>

*ii. Accidental Forfeiture of the Best Interest Contract Exemption in Case of a de Minimis Breach*

SEC staff raised a concern about language in the proposal’s Best Interest Contract Exemption, which required compliance with all applicable federal and state laws.<sup>85</sup> SEC staff warned that this requirement “could result in loss of exemption for trivial breaches,” and suggested that the Labor Department clarify that a *de minimis* breach would not disallow the exemption.<sup>86</sup> According to this language, if an advisor violated a state law unrelated to the contract or to the service of providing investment advice, the advisor would not be compliant with applicable state laws, which could technically result in loss of the exemption. For example, an advisor’s violation of a state law requiring a handicap-accessible ramp at the entrance to the building could result in loss of the exemption. The Labor Department attempted to implement the SEC staff’s suggestion,<sup>87</sup> but failed to resolve the problem. The SEC staff again recommended that the Labor Department make additional changes to this provision of the rule.<sup>88</sup> Career experts at the SEC later advised Labor Department officials that this problem had not been resolved, but the Labor Department failed to address the issue in the final proposal.<sup>89</sup>

Specifically, Section II(a) of the Best Interest Contract Exemption in the proposal requires that “the Advisor and Financial Institution enter into a written contract with the Retirement Investor that *incorporates the terms required by Section II(b)–(e).*”<sup>90</sup> Section II(d), in turn, requires that “[t]he Adviser, Financial Institution, and Affiliates will comply with all applicable federal and state laws.”<sup>91</sup> As such, by its terms, the Section could cause an advisor to forfeit the exemption for a small breach of state contract law.

Despite feedback from career, expert SEC staff regarding the inadequate revision three months in advance of the promulgation of the proposed rule,<sup>92</sup> the Labor Department declined to

<sup>84</sup> *Id.*

<sup>85</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234–003239.

<sup>86</sup> *Id.*

<sup>87</sup> *Id.* (responding that “as a result, failure to comply with law will not disallow the exemption”).

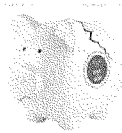
<sup>88</sup> Appendix B, Ex. 3, Email from Lona Nallengara, SEC, to Sharon Block, DOL (Jan. 26, 2015), SEC-DOL003274–003276.

<sup>89</sup> *Id.*

<sup>90</sup> Best Interest Contract Exemption § II(a), 80 Fed. Reg. 21,960, 21,984 (proposed Apr. 20, 2015) (to be codified at 29 C.F.R. pt. 2550) (emphasis added).

<sup>91</sup> Best Interest Contract Exemption § II(d)(1), 80 Fed. Reg. at 21,984.

<sup>92</sup> Appendix B, Ex. 3, Email from Lona Nallengara, SEC, to Sharon Block, DOL (Jan. 26, 2015), SEC-DOL003274–003276.



update the rule. Therefore, the proposed rule contains language that requires compliance with federal and state laws for application of the exemption<sup>93</sup> and creates the possibility of forfeiture of the exemption in case of a trivial breach.<sup>94</sup>

### iii. *Lack of a Cost-Benefit Analysis for Alternative Approaches*

The Labor Department rejected the SEC's recommendation to conduct quantitative analysis of the costs and benefits of alternative approaches to the rule, as required by Executive Orders (EOs) 12866 and 13563.<sup>95</sup> According to the Labor Department, expert, non-partisan, career SEC staff urged the Labor Department to "[c]onsider quantifying the costs and benefits of all the alternative approaches we considered and rejected."<sup>96</sup> The Department rejected the SEC expert's recommendation on the basis that its qualitative analysis sufficed:

We think this would be extraordinarily difficult and would appreciably delay the project for very little return. The extensive *qualitative* descriptions of the bases for rejecting the alternatives included in the current [regulatory impact analysis] effectively explain the bases for rejecting the alternative approaches. We would prefer to get feedback from OMB before undertaking any additional quantitative analyses.<sup>97</sup>

The Labor Department informed the Committee that following OMB's review of the rule, the Department declined to complete quantitative analysis because it found the regulatory impact analysis to be sufficiently "compelling."<sup>98</sup>

SEC staff also recommended that the Labor Department analyze the costs and risks associated with the possibility that the rule could decrease the availability of investment advice and could drive firms to switch to registered investment advisor models from broker-dealer models.<sup>99</sup> The Labor Department responded that the regulatory impact analysis addressed these

<sup>93</sup> Best Interest Contract Exemption § II(a), II(d)(1), 80 Fed. Reg. at 21,984.

<sup>94</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239.

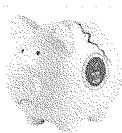
<sup>95</sup> Exec. Order No. 12866, 3 C.F.R. 638 (1994); Exec. Order No. 13563, 3 C.F.R. 215 (2012).

<sup>96</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239. From the context of the document, it appears that "we" as used in this quotation refers to the Labor Department, rather than the Labor Department and the SEC collectively. The document was prepared by the Labor Department and transmitted to the SEC. See Appendix B, Ex. 2, Email from Sharon Block, DOL, to Lona Nallengara, SEC (Jan. 9, 2015), SEC-DOL003234. Elsewhere in the document, the drafters used "we" to the exclusion of the SEC. See Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239 ("We have edited the language based on our conversations with SEC staff"; "We are confident that the language in the regulation lines up with the SEC and CFTC language, but are reaching out to the SEC regulatory team . . ."). Nowhere in the document is the Labor Department referenced similarly in the third person. Based on this contextual evidence, it appears that the phrasing of the SEC's comments is the Labor Department's articulation of the SEC's concerns, rather than the SEC's own words.

<sup>97</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239 (emphasis added).

<sup>98</sup> Briefing by Staff, DOL, to Committee Staff, HSGAC (Aug. 28, 2015) (notes on file with Committee).

<sup>99</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239.



issues, but that the Department was “reviewing to see if there is anything more . . . to say on the topic,”<sup>100</sup> and that it might “make additional edits after getting feedback from OMB.”<sup>101</sup> However, the Labor Department apparently did not conduct any additional follow-up work after OMB completed its review of the proposal.<sup>102</sup>

EOs 12866 and 13563 were enacted to improve the regulatory process. EO 12866 requires a federal agency to “assess all costs and benefits of available regulatory alternatives, including the alternative of not regulating,” and provides that the assessment should include “quantifiable measures.”<sup>103</sup> EO 13563, which supplements EO 12866, requires a federal agency to “tailor its regulations to impose the least burden on society,” to “choos[e] among alternative regulatory approaches,” and to “identify and assess available alternatives to direct regulation.”<sup>104</sup> EO 13563 also directs an agency to include “quantify[ing] anticipated present and future benefits and costs as accurately as possible.”<sup>105</sup> EOs 12866 and 13563 permit agencies to conduct qualitative analysis in place of quantitative analysis where the costs and benefits are “difficult or impossible to quantify.”<sup>106</sup> EO 13563 offers guidance on the types of factors that are difficult or impossible to quantify: “human dignity, fairness, and distributive impacts.”<sup>107</sup> Here, the costs and benefits associated with the Labor Department’s proposed fiduciary rule do not seem to meet the “difficult” or “impossible” threshold.

Additionally, OIRA issued a primer on EOs 12866 and 13563 to provide guidance to federal agencies in drafting a regulatory impact analysis.<sup>108</sup> OIRA emphasizes the importance of providing a quantitative analysis of alternatives and provides that agencies should conduct a quantitative analysis when at all possible.<sup>109</sup> For factors where quantification or monetization is not possible, OIRA instructs that the agency is not exempt from providing a quantitative analysis altogether and should still “present all available quantitative information.”<sup>110</sup> Like the Executive Orders, OIRA also provides examples of values that are not readily quantifiable, including privacy, dignity, ecological gains, improvements to quality of life, and aesthetic beauty.<sup>111</sup>

OIRA dedicates the large majority of the guidance to explaining, in great detail, how agencies should conduct quantitative analysis.<sup>112</sup> OIRA focuses in particular on factors that are

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> Briefing by Staff, DOL, to Committee Staff, HSGAC (Aug. 28, 2015) (notes on file with Committee).

<sup>103</sup> Exec. Order No. 12866 § 1(a), 3 C.F.R. 638 (1994).

<sup>104</sup> Exec. Order No. 13563 § 1(b)(3), (b)(5), 3 C.F.R. 215 (2012).

<sup>105</sup> *Id.* § 1(c).

<sup>106</sup> *Id.*

<sup>107</sup> *Id.*

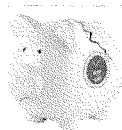
<sup>108</sup> OIRA, REGULATORY IMPACT ANALYSIS: A PRIMER.

<sup>109</sup> *Id.*

<sup>110</sup> *Id.* at 12.

<sup>111</sup> *Id.* at 12, 13.

<sup>112</sup> *See id.*



not easily quantified or monetized and on future projections and uncertainties.<sup>113</sup> Two full sections of the guidance are dedicated to analyzing “future benefits and costs” and “forecasts about the future.”<sup>114</sup> OIRA instructs that while forecasts about the future may be uncertain, those uncertainties should be analyzed—agencies should specify potential scenarios, calculate the benefits and costs associated with each scenario, and construct ranges of values.<sup>115</sup> OIRA further emphasizes that this is the minimum agencies should do, and that agencies should assign probabilities and calculate expected values based on those probabilities, if possible.<sup>116</sup>

The Executive Orders and the OIRA guidance do not exempt the Labor Department from conducting a quantitative analysis simply because the analysis would involve complicated calculations and future projections. The examples provided in the Executive Orders and the OIRA guidance indicate that factors that qualify as “difficult” or “impossible” to quantify are factors with inherently intangible or subjective properties.<sup>117</sup> Monetary costs and benefits very clearly do not fit into this category because they are both countable and objective. The fact that determining costs and benefits may involve complex calculations and future uncertainties is a distinguishable obstacle. In fact, OIRA emphasizes the importance of providing a quantifiable analysis, even when it involves complex calculations or future uncertainties.<sup>118</sup> While the Labor Department might not be able to capture every potential cost and benefit of the rule, OIRA’s guidance to agencies indicates that the Labor Department should have provided monetary and quantitative analysis of as many factors as possible. The Labor Department’s approach of determining that it would be difficult to calculate costs and benefits, and thus abandoning the effort altogether, starkly contrasts with the guidance provided by OIRA.

More broadly, the Labor Department’s dismissive response of the SEC experts’ recommendation calls into question the Department’s priorities in the rulemaking process and its commitment to thoughtfully considering the SEC staff’s input. The Labor Department’s decision to not undertake additional analysis following OMB’s review is indicative of the Department’s prioritization of accelerating its release of the proposal at the expense of a thorough process that appropriately reflected the input of the SEC staff.

**b. The Labor Department Failed to Incorporate Principles from Existing Federal Securities Laws and FINRA Rules**

FINRA—the Financial Industry Regulatory Authority—is the leading non-governmental regulator of brokerage firms and exchange markets and ensures that the security industry

<sup>113</sup> *See id.*

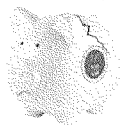
<sup>114</sup> *Id.* at 11, 12.

<sup>115</sup> *Id.*

<sup>116</sup> *Id.* at 14–15.

<sup>117</sup> *Id.* at 12, 13; Exec. Order No. 12866; Exec. Order No. 13563.

<sup>118</sup> OIRA, REGULATORY IMPACT ANALYSIS: A PRIMER, *supra* note 108.



operates fairly and honestly.<sup>119</sup> FINRA writes and enforces rules for every brokerage firm and broker in the United States, and also enforces federal securities laws and Municipal Securities Rulemaking Board (MSRB) rules.<sup>120</sup> FINRA has authority from the SEC to discipline brokers and brokerage firms for violations of FINRA rules, federal securities laws, and MSRB rules.<sup>121</sup> FINRA monitors more than 3,955 securities firms with approximately 643,320 brokers.<sup>122</sup>

In addition to ignoring substantive suggestions from subject-matter experts at the SEC, the Labor Department likewise apparently declined to incorporate existing federal securities laws and FINRA rules. Upon review of the proposed rule, FINRA provided critical feedback, stating that the rule “established principles that employ imprecise terms with little precedent in the federal securities laws or, in many cases, ERISA,” and that “[i]n some respects these principles even conflict with FINRA rules.”<sup>123</sup>

For example, FINRA highlighted that the proposed Best Interest Contract Exemption contains a provision that directly conflicts with FINRA rules.<sup>124</sup> Section III(a)(1) requires, prior to the purchase of a recommended asset, that an advisor project the total cost of investing in the asset for 1-, 5-, and 10-year periods, expressed as a dollar amount.<sup>125</sup> Such a projection requires the advisor to incidentally project investment performance because fees are tied to an asset’s value. This requirement directly conflicts with FINRA Rule 2210, which generally prohibits broker-dealers from making performance projections to the public.<sup>126</sup> Thus, by requiring advisors to project the future value of assets under management, the Labor Department’s rule would actually require advisors to violate FINRA rules.

The Labor Department’s failure to “build upon existing principles in the federal securities laws and FINRA rules”<sup>127</sup> is despite SEC staff urging the Labor Department to incorporate references to and aspects of federal securities laws and FINRA rules. In September and October 2014, SEC staff provided to the Labor Department, on multiple occasions, lists of relevant laws and rules, including rules from the Securities Act, Advisers Act, Exchange Act, FINRA, the National Association of Securities Dealers (NASD), and the Municipal Securities Rulemaking Board.<sup>128</sup>

<sup>119</sup> News Release, FINRA, NASD and NYSE Member Regulation Combine to Form the Financial Industry Regulatory Authority—FINRA (July 30, 2007); *About FINRA*, FINRA, <http://www.finra.org/about>.

<sup>120</sup> *What We Do*, FINRA, <http://www.finra.org/about/what-we-do>.

<sup>121</sup> News Release, FINRA (July 30, 2007), *supra* note 119; *About FINRA*, *supra* note 119.

<sup>122</sup> *For Industry Professionals*, FINRA, <https://www.finra.org/industry>.

<sup>123</sup> Appendix A, Ex. 26, FINRA Comments, at 11.

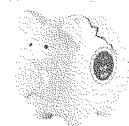
<sup>124</sup> *See id.* at 14.

<sup>125</sup> Best Interest Contract Exemption § III(a)(1), 80 Fed. Reg. 21,960, 21,985 (proposed Apr. 20, 2015) (to be codified at 29 C.F.R. pt. 2550) (emphasis added).

<sup>126</sup> FINRA, RULE 2210; Appendix A, Ex. 26, FINRA Comments, at 14.

<sup>127</sup> Appendix A, Ex. 26, FINRA Comments, at 11.

<sup>128</sup> Appendix B, Ex. 4, E-mail from Jennifer Porter, SEC, to Timothy Hauser, DOL (Sept. 4, 2014, 3:55 p.m.), SEC-DOL001768-001771; Appendix B, Ex. 5, E-mail from Jennifer Porter, SEC, to Timothy Hauser, DOL (Oct. 8, 2014, 10:35 a.m.), SEC-DOL001900-001901.





Additionally, SEC staff identified several items of concern relating to the Labor Department's lack of incorporation of federal securities laws and FINRA rules. For example, SEC staff recommended that the Labor Department redraft definitions in the disclosure requirements and document retention provisions so that the provisions expressly referenced SEC and FINRA definitions.<sup>129</sup> SEC staff reasoned that this would ensure that the Labor Department would receive complete and sufficiently comparable data from investment advisors.<sup>130</sup> However, the Labor Department dismissed the suggestion, instead merely including in the proposal's preamble a request for comment "as to whether the terms used and definitions are sufficient so that the information received will be reasonably comparable across different financial institutions."<sup>131</sup>

The Labor Department's failure to incorporate fundamental principles from federal securities laws and FINRA Rules further suggests that the Department did not thoroughly consult regulatory experts. This resulted in a rule that experts have highlighted as problematic, in part because of the conflicts it creates with existing and anticipated future regulatory frameworks.<sup>132</sup>

**c. The Labor Department Declined to Incorporate OIRA's Recommendations into the Proposed Rulemaking**

OIRA employs regulatory experts who carry out the office's mission as the federal government's chief review and oversight authority on Executive Branch rulemaking measures. Career, non-partisan, professional staff at OIRA conduct reviews of draft and final regulatory proposals, coordinate interagency review of proposals, consider and review comments from outside groups on proposed rulemakings, and offer guidance on how rulemakings can best achieve the intended purpose. In several instances, it appears that the Labor Department disregarded OIRA's recommendations and concerns about the Department's fiduciary rule.

The Labor Department declined OIRA's recommendation to add clarity to a particular provision of the rule. Specifically, OIRA instructed the Labor Department to add the qualifying adjective "all" to describe the types of common fee and compensation practices that the rule would preserve as exempt from ERISA's prohibited transactions rules.<sup>133</sup> OIRA proposed the following language: "the Department has worked to preserve beneficial models by separately proposing new exemptions from ERISA's prohibited transaction rules that will broadly permit firms to continue to *rely on all* common fee and compensation practices . . . ."<sup>134</sup> The Labor

<sup>129</sup> Appendix B, Ex. 2, Items of Concern Chart, SEC-DOL003234-003239.

<sup>130</sup> *Id.*

<sup>131</sup> *Id.*

<sup>132</sup> See Appendix A, Ex. 26, FINRA Comments, at 11.

<sup>133</sup> See Appendix B, Ex. 6, Conflict of Interest Rule, Apr. 8, 2015 Draft, EBSA Pass Back, SEC-DOL004832.

<sup>134</sup> *Id.*



Department rejected OIRA's changes and deleted "to rely on all," responding that "[n]ot all fee practices will be permitted by the exemptions" and explaining that, "[b]y deleting 'all' we slightly soften this by leaving it at 'common fee and compensation practices'"<sup>135</sup> This edit and the Department's explanation show that the Department envisioned the proposal as prohibiting some common fee and compensation packages.

The Labor Department's deletion of the word "all" raises questions about the Department's commitment to transparency. The language in the provision emphasizes that the Labor Department is committed to preserving existing models and to permitting the continuance of common fee and compensation practices. However, this language appears to be misleading because the Labor Department surreptitiously retained its ability to exclude some fee and compensation practices from the exemption. It is difficult to understand how the Labor Department sought to preserve and permit the current compensation structure in the industry when it explicitly envisioned the possibility of prohibiting some fee and compensation packages.

In another instance, OIRA questioned the Labor Department's use of the term "incidental advice" in connection with its discussion of the rule's seller's carve-out.<sup>136</sup> Regulatory experts at OIRA cautioned that exempting "incidental advice" could also "carve out advice given by a broker under the [guise] of being a mere order taker"<sup>137</sup> and noted, "[t]hat's where the SEC muddled the waters in the first place."<sup>138</sup> Documents received by the Committee contain no indication that the Labor Department fully responded to this concern.<sup>139</sup> Furthermore, this section of the preamble in the rule contains the same language as the draft rule,<sup>140</sup> showing that the Labor Department did not adjust the language to accommodate OIRA's concern, and further suggesting that the Labor Department did not thoroughly consider OIRA's comments.

**d. The Labor Department Did Not Fully Consider Concerns Raised by the Treasury Department**

The Treasury Department has enforcement authority over Individual Retirement Accounts (IRAs), which are a creation of the tax code, and thus the Labor Department's engagement with Treasury on the proposed rule is especially important. Given Treasury's authority and expertise in enforcing rules and regulations relating to IRAs, the Labor Department should have considered and remedied any concerns raised by Treasury officials about the proposed rule.

<sup>135</sup> *Id.* (emphasis added).

<sup>136</sup> *Id.* SEC-DOL004858.

<sup>137</sup> *Id.*

<sup>138</sup> *Id.* (emphasis added).

<sup>139</sup> *Id.*

<sup>140</sup> Conflict of Interest Rule—Retirement Investment Advice § (b)(1)(i), 80 Fed. Reg. 21,928, 21,957 (proposed Apr. 20, 2015) (to be codified at 29 C.F.R. pts. 2509, 2510).



Treasury officials and other experts have raised concerns about the Best Interest Contract Exemption (BIC exemption), because it would impose new requirements on fiduciaries with respect to IRAs.<sup>141</sup> IRAs are governed by the Internal Revenue Code, not by ERISA. Unlike ERISA, the Internal Revenue Code “does not directly impose responsibilities of prudence and loyalty on fiduciaries.”<sup>142</sup> The Labor Department’s rule, however, would create such responsibilities by requiring fiduciaries “to act in accordance with the Impartial Conduct Standards in transactions governed by the exemptions.”<sup>143</sup> The rule’s background section acknowledges that the proposal would more significantly increase requirements for advisors with respect to IRAs than it would for advisors of accounts governed by ERISA (the Employee Retirement Income Security Act) because ERISA already requires those advisors to meet prudence and loyalty standards.

Former Assistant Secretary of Labor Bradford Campbell criticized this aspect of the rule as an effort by the Labor Department to sidestep Congress, stating that “[d]espite their simultaneous creation in 1974, Congress expressly chose not [to] apply the ERISA fiduciary standard to IRAs.”<sup>144</sup> According to Mr. Campbell, “the Department is attempting to do something through [the proposed rule] that Congress explicitly chose not to do.”<sup>145</sup>

Treasury officials similarly voiced concerns about the Labor Department extending the reach of the rule to IRAs. Treasury officials commented that earlier amendments were made “to reflect Congressional intent,” on the basis that Congressional intent was “being undermined by rules that [were] not reflective of current market practices.”<sup>146</sup> Treasury officials argued that this amendment, by imposing requirements with respect to accounts governed by a different statute and under the jurisdiction of a different federal agency, “seems to fly in the face of the logic . . . that these amendments are necessary to reflect Congressional intent.”<sup>147</sup> The Labor Department responded by disagreeing and effectively dismissing the Treasury Department’s concern. The Labor Department wrote:

We think there’s a difference here between the regulation and the exemptions. The purpose of the regulation expanding the definition of ‘fiduciary’ is to reflect Congressional intent. However, the purpose of this exemption is to say that if

<sup>141</sup> Appendix B, Ex. 7, Proposed Amendments to Class Exemptions, Apr. 21, 2015 Draft, Treasury Comments (Mar. 21, 2015), SEC-DOL005312.

<sup>142</sup> *Id.* (emphasis added).

<sup>143</sup> CONG. RESEARCH SERV., DOL’S 2015 PROPOSED FIDUCIARY RULE ON INVESTMENT ADVICE, IN FOCUS, IF10318, Nov. 12, 2015. The Impartial Conduct Standards require an advisor to act in the best interest of the client-investor and not to accept more than reasonable compensation.

<sup>144</sup> House Ways & Means Committee Hearing, *supra* note 47 (statement of Bradford Campbell).

<sup>145</sup> *Id.*

<sup>146</sup> Appendix B, Ex. 7, Conflict of Interest Rule, Treasury Comments, Mar. 21, 2015, SEC-DOL005312.

<sup>147</sup> *Id.*



you're a fiduciary under the [Internal Revenue Code] (and Congressional intent), and want to receive variable compensation, then you have to comply with these conduct standards, even if they are not independently imposed by Congress.<sup>148</sup>

IRA advisors receive variable compensation, especially when providing advice to low- and middle-income investors.<sup>149</sup> Thus, IRA advisors would be subject to the rule's conduct standards. Despite Congress' intent to regulate IRA advisors under a different law, the Labor Department would regulate them using variable compensation as a proxy.

In a letter to Chairman Johnson on December 14, 2015, Treasury Department Assistant Secretary for Legislative Affairs, Anne Wall, stated that "Treasury believes that DOL appropriately considered Treasury's comments on the drafts during the OIRA process, including the comments specified in your letter" (and quoted above).<sup>150</sup> However, based on the documents, it is unconvincing that the Labor Department fully considered the comments of the Treasury Department experts. First, documents the Committee received provide no indication that the Departments discussed the Treasury Department's concern beyond the Labor Department's initial response to the Treasury Department, where it merely disagreed with Treasury's comment. Second, the Labor Department promulgated the proposed rule less than two weeks after circulating this draft and the accompanying comments, undoubtedly limiting the extent to which the Labor Department considered the comments it received from the Treasury Department experts on the draft. Finally, the promulgated proposal does not contain language signifying that the Labor Department edited the rule in accordance with the Treasury Department's stated concerns. For these reasons, it is difficult to conclude objectively that the Labor Department fully considered the Treasury Department's comments.

### III. EXPERTS HAVE EXPRESSED CONCERNS ABOUT THE RULE'S ANTICIPATED HARM TO MIDDLE-INCOME AND SMALL BUSINESS INVESTORS

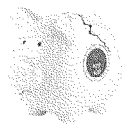
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Chairman Johnson's inquiry raises concerns about both the process and the substance of the Labor Department's rulemaking. The Committee has received documents that demonstrate that the Labor Department prioritized expediting the drafting process at the expense of thoughtfully considering and addressing concerns from industry experts. In multiple instances, the Department disregarded advice from the SEC, OIRA, and Treasury, and failed to undertake a thorough cost-benefit analysis of the rule. The majority staff finds these actions especially

<sup>148</sup> *Id.*

<sup>149</sup> Appendix A, Ex. 27, Letter from Commonwealth Financial Network to DOL (July 21, 2015).

<sup>150</sup> Appendix A, Ex. 28, Letter from Hon. Anne Wall, Asst. Sec'y for Leg. Affairs, Dep't of the Treasury, to Chairman Johnson (Dec. 14, 2015).



troubling because of the concerns raised about the risk of the rule's anticipated harm to middle-income investors.

Generally, industry experts, including investment advisors, support a best interest standard, but have criticized the rule on the grounds that it is overly complex and burdensome. For example, Peter Schneider, the President of Primerica, testified to Congress that he "agree[s] that firms and their representatives should always act in their clients' best interests."<sup>151</sup> He explained that he is concerned "that the requirements and uncertainties of the [Best Interest Contract Exemption] are so complex and burdensome that the exemption is n either administratively nor operationally feasible."<sup>152</sup>

Similarly, former SEC Commissioner Daniel Gallagher has harshly criticized the rule, calling it a "mess," in part because advisors who adhere to a best interest standard still risk noncompliance with the rule because of its many complicated requirements.<sup>153</sup> Commissioner Gallagher has cautioned that the Labor Department's rule would result in the "elimination of an entire class of accounts" for investors and would subject advisors to "unlimited liability."<sup>154</sup> Other experts and observers have also raised concerns that the conditions and requirements the rule imposes are ambiguous and unworkable, which will increase litigation risk and regulatory costs. Experts anticipate that advisors will incur initial compliance costs of \$21.5 million and annual maintenance costs of \$5.1 million, resulting in increased costs for retail investment advice by 73% to 196% as a result of the Labor Department's proposal.<sup>155</sup>

Additionally, experts contend that the Administration has inflated the harm that results from investors relying on "conflicted advice." The White House and the Labor Department claim that conflicted advice from brokers costs investors \$17 billion per year.<sup>156</sup> Former SEC chief economist Craig Lewis has explained that the \$17 billion estimate is based on a calculation that failed to account for discrepancies in the data and that used outdated data from the 1990s

<sup>151</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Peter Schneider); *see also id.* (statement of Robert Litan) ("[T]he notion that all retirement investment advisers should be held to a best interest of client standard is not controversial.").

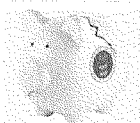
<sup>152</sup> *Id.*; House Ways & Means Committee Hearing, *supra* note 47 (statement of Judy VanArsdale, Co-Owner, enrich Private Wealth Management).

<sup>153</sup> Mark Schoeff Jr., *SEC Commissioner: DOL Fiduciary Rule Would Create "a Mess"*, INVESTMENT NEWS (Aug. 4, 2015, 1:18 PM), <http://www.investmentnews.com/article/20150804/FREE/150809978/sec-commissioner-dol-fiduciary-rule-would-create-a-mess>.

<sup>154</sup> *Id.*; Speech to the Chamber of Commerce, Daniel Gallagher, Comm'r, SEC (Aug. 4, 2015), *available at* <https://www.uschamber.com/event/discussion-sec-commissioner-daniel-gallagher>.

<sup>155</sup> MILLOY, AM. ACTION FORUM, *supra* note 43; *see also* DELOITTE DEVELOPMENT LLC, REPORT ON THE ANTICIPATED OPERATIONAL IMPACTS TO BROKER-DEALERS OF THE DEPARTMENT OF LABOR'S PROPOSED CONFLICT OF INTEREST RULE PACKAGE (2015) (reporting similar findings).

<sup>156</sup> EXEC. OFFICE OF THE PRESIDENT, THE EFFECTS OF CONFLICTED INVESTMENT ADVICE ON RETIREMENT SAVINGS (2015).



and 2000s.<sup>157</sup> Mr. Lewis stated, “[y]ou don’t have to be an economist to recognize the Administration’s \$17 billion talking point significantly overestimates the costs, if any, to investors relying on the ‘conflicted advice’ of brokers.”<sup>158</sup>

Experts have focused, in particular, on the negative impact that the rule will have on small-account owners—small businesses and middle-income investors. The Small Business Administration has commented that the rule “would likely increase the costs and burdens associated with servicing smaller plans . . . [which] could limit financial advisers’ ability to offer savings and investment advice to clients . . . [which] could ultimately lead advisors to stop providing retirement services to small businesses.”<sup>159</sup> Similarly, former Assistant Secretary of Labor Bradford Campbell testified that the rule “likely will harm the very retirement investors it is intended to help.”<sup>160</sup> Mr. Campbell echoed the Small Business Administration’s concerns that the rule will increase the cost and reduce the availability of advice to small plans and small-account IRA owners.<sup>161</sup> Finally, experts have pointed to an “advice gap” that has developed in the United Kingdom (U.K.) as a result of a 2013 rule change in the U.K. that is effectually identical to the Labor Department’s rule.<sup>162</sup> According to ERISA experts, it is “widely accepted in the U.K.” that “middle- and lower- income savers in the U.K. are being cut off from investment advice.”<sup>163</sup> The United Kingdom government has “launched a major review of exactly that advice gap.”<sup>164</sup>

First, the rule contains a carve-out that will not apply to small businesses. The “Seller’s Carve-Out” exempts an investment advisor from fiduciary duties when the advisor sells or markets materials, as long as the advisor discloses that the advisor is paid to sell proprietary financial product and is not providing fiduciary advice.<sup>165</sup> However, the proposal prohibits advisors to small businesses from using the Seller’s Carve-Out based on the assumption that small businesses lack financial sophistication.<sup>166</sup> Small businesses and ERISA experts have voiced concerns that the rule will deprive small businesses of access to guidance on investment

<sup>157</sup> Craig M. Lewis, *An Inflated \$17 Billion Talking Point From the DOL*, FORBES (Dec. 16, 2015, 12:30 PM), <http://www.forbes.com/sites/realspin/2015/12/16/an-inflated-17-billion-talking-point-from-the-dol/#782b028439e1>.

<sup>158</sup> *Id.*

<sup>159</sup> Appendix A, Ex. 29, Letter from Claudia Rodgers, Acting Chief Counsel for Advocacy, and Dillon Taylor, Asst. Chief Counsel for Advocacy, Small Business Admin., to Hon. Phyllis Borzi, Asst. Sec’y, EBSA, DOL, at 5–6 (July 17, 2015).

<sup>160</sup> House Ways & Means Committee Hearing, *supra* note 47 (statement of Bradford Campbell).

<sup>161</sup> *Id.*

<sup>162</sup> KENT MASON, DAVIS & HARMAN LLP, U.K. LAUNCHES REVIEW OF “ADVICE GAP” FOR SMALL ACCOUNTS FOLLOWING A 2013 RULE CHANGE WITH EFFECTS IDENTICAL TO WHAT DOL NOW PROPOSES (2015).

<sup>163</sup> *Id.*

<sup>164</sup> *Id.*

<sup>165</sup> Conflict of Interest Rule—Retirement Investment Advice § (b)(1)(i), 80 Fed. Reg. 21,928, 21,957 (proposed Apr. 20, 2015) (to be codified at 29 C.F.R. pts. 2509, 2510) (Seller’s Carve-Out); *id.* pmbl. § IV(C)(1)(a) at 21,941–42 (explaining the Seller’s Carve-Out).

<sup>166</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Darlene Miller, President & CEO, Permac Industries, Board Member, U.S. Chamber of Commerce).



options that are otherwise permitted by the carve-out.<sup>167</sup> Small businesses have additionally refuted the Labor Department's flawed assumption that small businesses lack the requisite sophistication to engage with investment advisors without statutorily imposed protections.<sup>168</sup> At a hearing before the Senate Committee on Health, Education, Labor and Pensions, a small-business owner testified:

I would not be able to run a successful business if I were not able to understand when I am involved in a sales discussion. . . . The assumption that small plans, participants and IRA owners cannot understand the difference between sales and advice does not match my real world experience. The [Labor] Department can protect participants, IRA owners and small plans with the same kind of disclosures that it requires of large plans under the large plan carve out, but without eliminating their right to choose the services and products that best fit their needs.<sup>169</sup>

Former Assistant Secretary Campbell similarly criticized the carve-out, stating "there is no clear basis to believe that plan size is a proxy for financial sophistication, and no basis to treat every IRA owner as if she is incapable of making informed choices."<sup>170</sup>

Additionally, experts have voiced concerns that the Best Interest Contract Exemption (BIC exemption) is unworkable and that firms will not use it. The BIC exemption allows certain broker-dealers and other fiduciaries to receive compensation that would otherwise be prohibited, such as commissions.<sup>171</sup> To take advantage of the BIC exemption, the investor and advisor must sign a contract acknowledging fiduciary status.<sup>172</sup> The advisor must act in the best interest of the client and must make numerous disclosures to the client and to the Labor Department.<sup>173</sup> Experts contend that the BIC exemption is unworkable and will increase the cost of investment advice and services and will, consequently, decrease access to investment services for small investors.<sup>174</sup> Experts explain that the BIC exemption imposes conditions and requirements for advisors that are ambiguous, creating uncertainty and putting advisors at risk for penalties and lawsuits, including class action lawsuits.<sup>175</sup> Industry participants caution that investment firms will consequently decline to use the BIC exemption.<sup>176</sup>

<sup>167</sup> *Id.*

<sup>168</sup> *Id.*

<sup>169</sup> *Id.*

<sup>170</sup> *Id.* (statement of Bradford Campbell).

<sup>171</sup> CONG. RESEARCH SERV., DOL'S 2015 PROPOSED FIDUCIARY RULE ON INVESTMENT ADVICE, IN FOCUS, IF10318, Nov. 12, 2015.

<sup>172</sup> *Id.*

<sup>173</sup> *Id.*

<sup>174</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Darlene Miller).

<sup>175</sup> *Id.* (statements of Darlene Miller and Peter Schneider).

<sup>176</sup> *Id.*; House Ways & Means Committee Hearing, *supra* note 47 (statements of Judy VanArsdale and Bradford Campbell).



According to experts, the unworkability of the BIC exemption will inhibit middle-income, small-account owners' access to investment services. Experts explain that firms that do not use the exemption will likely convert their commission-based brokerage IRAs to fee-based accounts.<sup>177</sup> Fee-based accounts are more expensive to operate than commission-based accounts and, therefore, often require account minimums of \$25,000 and higher annual fees.<sup>178</sup> Experts caution that these costs will inhibit access to investment services for small account owners and could result in losses in retirement savings of as much as \$68–80 billion per year.<sup>179</sup> Even in the case of advisors who continue to provide services to small account owners, flat fees will present affordability challenges for middle-income investors who cannot afford to pay flat rates and currently rely on commission-based fees.<sup>180</sup>

Supporters of the rule have criticized large, publicly-traded investment firms for publicly predicting significant negative consequences, while simultaneously “assuring [investors] that the rule will have no significant impact on their companies” and that they “are well-positioned to ‘adapt to any regulatory framework that emerges.’”<sup>181</sup>

However, these large investment firms are not the ones that will feel the most significant effects of the rule. Rather, the rule is likely to harm small- and mid-size investment firms. For example, Judy VanArsdale, the co-owner of a seven-employee wealth management company, testified before the House Committee on Ways and Means about her concerns about the rule.<sup>182</sup> As a small wealth management company, Ms. VanArsdale’s company serves more than 2,500 accounts, with more than 800 accounts containing less than \$25,000.<sup>183</sup> Ms. VanArsdale explained that the rule increases litigation risk because of its lack of clarity and its creation of state-law class action lawsuits.<sup>184</sup> Ms. VanArsdale stated that, as a small-business owner, she feels “great concern over subjecting [her] business to increased business and litigation risk.”<sup>185</sup> According to Ms. VanArsdale, to avoid litigation risk, “small businesses . . . may not feel comfortable using the BIC exemption, and . . . would be restricted from serving retirement brokerage accounts.”<sup>186</sup> While large firms may be better suited to withstand changes in the

<sup>177</sup> Senate HELP Committee Hearing, *supra* note 2 (statements of Darlene Miller and Peter Schneider); House Ways & Means Committee Hearing, *supra* note 47 (statement of Bradford Campbell).

<sup>178</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Peter Schneider); House Ways & Means Committee Hearing, *supra* note 47 (statement of Bradford Campbell).

<sup>179</sup> QUANTRIA STRATEGIES, *supra* note 13, at 1.

<sup>180</sup> Senate HELP Committee Hearing, *supra* note 2 (statement of Peter Schneider).

<sup>181</sup> Appendix A, Ex. 30, Letter from Hon. Elizabeth Warren, U.S. Sen., and Hon. Elijah Cummings, U.S. House of Representatives, to Sec’y Perez, DOL, and Hon. Shaun Donovan, Dir., OMB (Feb. 11, 2016).

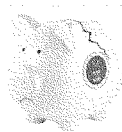
<sup>182</sup> House Ways & Means Committee Hearing, *supra* note 47 (statement of Judy VanArsdale).

<sup>183</sup> *Id.*

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

<sup>186</sup> *Id.*





regulatory regime, small- and mid-size investment firms—and the middle-class consumers they service—have less tolerance to weather such changes.

#### IV. THE ADMINISTRATION WAS PREDETERMINED TO REGULATE THE INDUSTRY AND SOUGHT EVIDENCE TO JUSTIFY ITS PREFERRED ACTION

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The Labor Department refused to provide the Committee with its communications with the White House. However, the Committee obtained some of these communications from another party. The communications indicate that the Labor Department and the White House were predetermined to regulate the industry and sought evidence to justify their preferred action. The communications also suggest that the White House may have played an outsized role in the rulemaking, in conflict with the Administrative Procedure Act.

In an email to Brian Deese—a senior political advisor in the Executive Office of the President—a Labor Department policy advisor wrote of the “challenges in completing the [regulatory impact analysis].”<sup>187</sup> In particular, he noted, “we need to determine whether the available literature, our work with RAND, and any other data we have not yet identified can be woven together to demonstrate that there is a market failure and to monetize the potential benefits of fixing it.”<sup>188</sup> In another email to Mr. Deese, a Labor Department policy advisor discussed plans for packaging the rulemaking re-proposal.<sup>189</sup> The email noted a GAO report that the Labor Department intended to use to “build[] the case for why the rule is necessary.”<sup>190</sup>

EOs 12866 and 13563—enacted to reform and improve regulations and the regulatory process—require agencies to identify a market failure or other compelling problem that justifies regulation before the agency begins the regulatory drafting process. Specifically, EO 12866 provides that agencies should promulgate regulations only if they are “made necessary by compelling public need, such as material failures of private markets.”<sup>191</sup> EO 12866 further provides that “in deciding whether and how to regulate, agencies should assess all costs and benefits of available regulatory alternatives, including the alternative of not regulating.”<sup>192</sup> However, as evidenced by these emails, the Labor Department and the White House worked

<sup>187</sup> Appendix B, Ex. 8, E-mail from Zachary A. Epstein, DOL, to Brian C. Deese, Exec. Office of the President, et al. (Oct. 25, 2011, 7:30 PM), SEC-DOL005872–005873.

<sup>188</sup> *Id.*

<sup>189</sup> Appendix B, Ex. 9, Email from Chris Cosby, DOL, to Brian C. Deese, Exec. Office of the President, et al. (Nov. 2, 2011, 5:47 PM), SEC-DOL006041–006042.

<sup>190</sup> *Id.*

<sup>191</sup> Exec. Order No. 12866 § 1(a), 3 C.F.R. 638 (1994); *see also* Exec. Order No. 13563 § 1(b), 3 C.F.R. 215 (2012) (providing that an agency must “propose or adopt a regulation only upon a reasoned determination that its benefits justify its costs”).

<sup>192</sup> Exec. Order No. 12866 § 1(a), 3 C.F.R. 638 (1994).



backwards—they first determined that they wanted to create the rule, then searched for evidence to justify it. The way in which the Labor Department and the White House approached the regulatory impact analysis is opposite to the methodology required by executive order.

The Administrative Procedure Act vests control of a rulemaking in the agency proposing the regulation. The Executive Office of the President—including OIRA, the National Economic Council, and other entities—exists to coordinate policy broadly across the executive branch, but ultimately each agency owns its particular rulemaking. With respect to the Labor Department’s fiduciary rulemaking, it appears that the White House may have played an outsized role.

Documents that the Committee received suggest that the proposal was initially driven by political appointees in the Executive Office of the President. First, the level of detail in email communications between the Labor Department and the White House indicates that White House advisors may have exceeded their coordination function in drafting the rule. For instance, in the email discussing a GAO report that the Labor Department felt could build a case for the rule, a Labor Department official provided specific page numbers and direct quotations from the report to the White House’s Brian Deese.<sup>193</sup> Such detail suggests that Mr. Deese, and other policy advisors within the White House, were involved in crafting the basis for the rule and the regulatory impact analysis on a granular and collaborative basis.

Additionally, in October and November 2011, the White House’s National Economic Council convened a series of meetings among the Labor Department, the SEC, the Treasury Department, and the White House to discuss the rule’s economic analysis.<sup>194</sup> These discussions appear to have been more than mere coordination meetings. Rather, it seems that White House officials were involved in developing material to justify the need for the Labor Department’s proposal.

Moreover, Assistant Secretary of Labor Phyllis Borzi, who has been described as the “main architect” of the fiduciary rule,<sup>195</sup> ranks as the twelfth most frequent visitor to the White House during the Obama Administration.<sup>196</sup> Since 2009, Ms. Borzi has visited the White House

<sup>193</sup> *Id.*

<sup>194</sup> Brian Deese, then-Deputy Director of the National Economic Council, and Adriana Kugler, then-Chief Economist to then-Department of Labor Secretary Hilda Solis, hosted meetings at the White House in October and November 2011. White House staff, Labor Department staff, SEC staff, and Treasury Department staff attended the meetings. See Appendix B, Ex. 10, Email from Jessica Schumer, Exec. Office of the President, to Brian C. Deese et al. (Oct. 12, 2011) (October 20, 2011 meeting), SEC-DOL005698; Appendix B, Ex. 11, Email from Jessica Schumer to Brian C. Deese et al. (Oct. 25, 2011) (October 27, 2011 meeting), SEC-DOL005861; Appendix B, Ex. 9, Email from Chris Cosby, DOL, to Brian C. Deese et al. (Nov. 2, 2011) (November 2, 2011 meeting), SEC-DOL006041.

<sup>195</sup> Melanie Waddell, *DOL to ‘Simplify and Streamline’ Fiduciary Rule: Borzi*, THINKADVISOR (Oct. 20, 2015).

<sup>196</sup> Jason Howerton, *Here Are the 25 People Who Have Visited the Obama White House the Most* (Feb. 8, 2016, 1:38 PM), <http://www.theblaze.com/stories/2016/02/08/here-are-the-25-people-who-have-visited-the-obama-white-house-the-most-no-3-is-apparently-shrouded-in-mystery/>.



338 times.<sup>197</sup> Two other senior Labor Department officials rank as the ninth and sixth most frequent White House visitors, with 369 and 376 visits, respectively.<sup>198</sup>

Finally, a White House memorandum entitled “Draft Conflict of Interest Rule for Retirement Savings” further illustrates the White House’s significant involvement in the rulemaking process. The memorandum, circulated by White House Council of Economic Advisors Chairman (CEA) Jason Furman and CEA member Betsey Stevenson, to the President’s senior advisors including John Podesta, Susan Rice, Jennifer Palmieri, and Valerie Jarrett, criticized current regulations relating to investment advice on retirement accounts.<sup>199</sup> The memorandum argued that aggressive regulatory action was necessary to remedy the inadequate existing consumer protections on investment advice.<sup>200</sup> The Department issued its proposal just four months later.

#### V. THE ADMINISTRATION OBSTRUCTED CHAIRMAN JOHNSON’S INQUIRY BY LIMITING THE INFORMATION THE COMMITTEE WAS ABLE TO OBTAIN

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In the course of conducting oversight on the Labor Department’s rulemaking, Chairman Johnson experienced tremendous opposition and noncooperation from the Administration. The Labor Department withheld documents and even went so far as to urge the SEC—an independent agency that is designed to be bipartisan—to do the same. OIRA also withheld documents. The Labor Department’s and OIRA’s refusals to fully cooperate with Chairman Johnson’s oversight has prevented the Committee from obtaining relevant documents and has hindered the Chairman’s overall inquiry.

##### a. The Labor Department Remains Uncooperative with Chairman Johnson’s Requests for Information and Documents from February 2015

Chairman Johnson wrote a letter to the Labor Department on February 5, 2015, requesting information and documents relating to the Department’s anticipated rule.<sup>201</sup> After the Labor Department failed to produce communications in response to his request, Chairman Johnson reiterated the requests in another letter on March 17, 2015.<sup>202</sup> Chairman Johnson requested communications about the Labor Department’s rulemaking between the Labor

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<sup>197</sup> *Id.*

<sup>198</sup> *Id.*

<sup>199</sup> Memorandum from Jason Furman, Chairman, White House Council of Econ. Advisors, and Betsey Stevenson, Member, White House Council of Econ. Advisors, to White House Senior Advisors (Jan. 13, 2015).

<sup>200</sup> *Id.*

<sup>201</sup> Appendix A, Ex. 1, Letter from Chairman Johnson to Sec’y Perez, DOL (Feb. 5, 2015).

<sup>202</sup> Appendix A, Ex. 2, Letter from Chairman Johnson to Sec’y Perez, DOL (Mar. 17, 2015).



Department and the SEC and between the Labor Department and the White House.<sup>203</sup> By its own admission, the Department has not produced all material responsive to Chairman Johnson's requests.<sup>204</sup>

Specifically, the Labor Department has not produced any material responsive to Chairman Johnson's request for communications between the Department and the White House.<sup>205</sup> In August 2015, Chairman Johnson signaled his objection to Adri Jayaratne's nomination to be the Labor Department's Assistant Secretary for Congressional and Intergovernmental Affairs because of the Department's failure—under Mr. Jayaratne's time as acting head of the Office of Congressional and Intergovernmental Affairs—to respond fully to the Chairman's requests. Subsequently, the Labor Department informed the majority staff that no responsive documents existed.<sup>206</sup> The Labor Department, however, refused to explain how the Department came to this conclusion or what type of search the Department conducted.<sup>207</sup> The Committee later received, from another source, some communications between the Department and the White House about the rulemaking.<sup>208</sup> Still, later, in December 2015, the Labor Department again refused to provide the requested materials and declined to confirm whether it had sought consent from the White House to produce the material.<sup>209</sup>

The Labor Department has not fully responded to Chairman Johnson's request for communications between the Department and the SEC. The Labor Department has produced only a limited subset of self-selected communications between the Department and the SEC and provided short briefings.<sup>210</sup> The communications the Labor Department produced are mostly

<sup>203</sup> *Id.*

<sup>204</sup> Chairman Johnson did not request to conduct transcribed interviews with Labor Department officials. In light of the Labor Department's repeated refusals to produce requested information and documents, its interference with the SEC's response to the Chairman's separate request to the SEC, and the Department's overall obstructive posture with respect to the Chairman's inquiry, it is likely that requests for transcribed interviews would have proved futile.

<sup>205</sup> Email from Committee Staff, HSGAC, to Kathryn Garza-Ahlgren, DOL (Aug. 24, 2015, 2:00 PM) (on file with Committee).

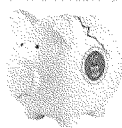
<sup>206</sup> Phone Call between Committee Staff, HSGAC, and DOL (Aug. 5, 2015); *see also* Email from Committee Staff, HSGAC, to Nikki McKinney, DOL (Dec. 17, 2015, 1:19 PM) (on file with Committee) (referencing the phone call); Email from Committee Staff, HSGAC, to Kathryn Garza-Ahlgren, DOL (Aug. 24, 2015, 2:00 PM) (on file with Committee) (referencing the phone call).

<sup>207</sup> Phone Call between Committee Staff, HSGAC, and DOL (Aug. 2015); *see also* Email from Committee Staff, HSGAC, to Nikki McKinney, DOL (Dec. 17, 2015, 1:19 PM) (on file with Committee) (referencing the phone call); Email from Committee Staff, HSGAC, to Kathryn Garza-Ahlgren, DOL (Aug. 24, 2015, 2:00 PM) (on file with Committee) (referencing the phone call).

<sup>208</sup> The SEC produced to the Committee on November 23, 2015, documents containing communications between the Labor Department and the White House. *See* Email from Committee Staff, HSGAC, to Nikki McKinney, DOL (Dec. 17, 2015, 1:19 PM) (on file with Committee).

<sup>209</sup> Phone Call between Committee Staff, HSGAC, and DOL (Dec. 17, 2015); Email from Committee Staff, HSGAC, to Nikki McKinney, DOL (Dec. 17, 2015, 1:19 PM) (on file with Committee); Email from Committee Staff, HSGAC, to Nikki McKinney, DOL (Jan. 12, 2016, 12:52 PM) (on file with Committee).

<sup>210</sup> Appendix C, Dep't of Labor Document Production, DOL000001-002458; Emails between Committee Staff, HSGAC, and Elva Linares, DOL (Aug. 26-27, 2015) (on file with Committee). Mr. Jayaratne's staff, moreover,



related to scheduling meetings and do not address substantive aspects of the rule drafting process.<sup>211</sup> Moreover, the Department only produced these documents after the Chairman made a separate but similar request to the SEC for documents.<sup>212</sup> Additionally, during the briefings, Labor Department lawyers unilaterally limited the subject matter and timing of the briefings, leaving many questions unanswered.

Regarding the Labor Department and SEC communications, the Labor Department refused to certify that the communications produced to the Committee constituted the full universe of communications responsive to the Chairman's request.<sup>213</sup> Furthermore, the Labor Department refused to provide information about the total number of responsive documents, or the methods the Department used to identify responsive material.<sup>214</sup> The majority staff has confirmed that these communications, in fact, do *not* constitute the full universe of responsive communications. Rather, it appears that the Labor Department combed through its communications with the SEC and deliberately omitted the large majority of communications that would inform Chairman Johnson's inquiry. The Committee has obtained documents from another source that contain many communications between the Labor Department and the SEC that the Department omitted from its production. The Labor Department has acknowledged to the majority staff that additional responsive material exists, though it refuses to produce such material.<sup>215</sup>

In July 2015, Chairman Johnson spoke with Secretary Perez about the outstanding document requests. The majority staff has also communicated directly with Mr. Jayaratne about the Labor Department's unsatisfactory responses. Despite these interactions, and Chairman Johnson's continued objection to Mr. Jayaratne's confirmation by the Senate, the Labor Department still refuses to comply fully with the Chairman's requests. It seems that the Labor Department has only seriously engaged in discussions about fully satisfying Chairman Johnson's requests in an effort to advance Mr. Jayaratne's nomination. Ultimately, though, the Labor Department remains unwilling to produce all responsive documents to the Committee.

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placed unilateral time and content restrictions on these briefings, refusing to answer questions that they deemed outside the scope of the briefings. Emails between Committee Staff, HSGAC, and Elva Linares, DOL (Aug. 26–27, 2015) (on file with Committee).

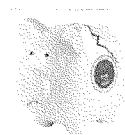
<sup>211</sup> Appendix C, Dep't of Labor Document Production, DOL000001–002458.

<sup>212</sup> Email from Committee Staff, HSGAC, to Adri Jayaratne, Acting Asst. Sec'y, Office of Cong. & Intergovernmental Affairs, DOL (July 8, 2015, 6:56 PM) (on file with Committee).

<sup>213</sup> Email from Kathryn Garza-Ahlgren, DOL, to Committee Staff, HSGAC (Aug. 21, 2015, 5:14 PM) (on file with Committee).

<sup>214</sup> Email from Committee Staff, HSGAC, to Adri Jayaratne, Acting Asst. Sec'y, Office of Cong. & Intergovernmental Affairs, DOL (July 8, 2015, 6:56 PM) (on file with Committee); Email from Committee Staff, HSGAC, to Kathryn Garza-Ahlgren, DOL (Aug. 24, 2015, 2:00 PM) (on file with Committee).

<sup>215</sup> Email from Kathryn Garza-Ahlgren, DOL, to Committee Staff, HSGAC (Aug. 21, 2015, 5:14 PM) (on file with Committee).



Finally, despite repeatedly refusing to produce responsive material, the Labor Department has not asserted any claim of privilege on the withheld material, and has refused to provide basic information about the scope, nature, and contents of the withheld material.<sup>216</sup> The Labor Department's stated reasons for noncompliance are all the more concerning given that its regulatory authority derives from an express grant of legislative authority from Congress to the Department. Congress—and, in particular, this Committee—retain broad oversight authority over the Labor Department's regulatory process and procedures. Ultimately, Congress also retains the authority to reject the Labor Department's rule through the Congressional Review Act.<sup>217</sup> Accordingly, the Committee ought to have access—and the Labor Department should be completely willing to provide access—to all documents and communications related to the rulemaking.

With little cooperation from the Labor Department, Chairman Johnson wrote to other agencies to seek information about the rulemaking. Under pressure from Chairman Johnson and after the Chairman threatened to compel production of the material,<sup>218</sup> the SEC ultimately provided a number of documents to the Committee that offered tremendous insight into the rulemaking. Similarly, FINRA also voluntarily assisted in providing useful information.

**b. The Labor Department Attempted to Interfere with the SEC's Cooperation with the Chairman's Requests**

In addition to withholding information from the Committee, the Labor Department admitted to Chairman Johnson that it had urged the SEC—an independent commission set up to be free of political pressure from the Executive Branch—to disregard Chairman Johnson's requests that he made separately to the SEC for documents in the SEC's possession and control.<sup>219</sup> Chairman Johnson made those requests to the SEC precisely because the Labor Department had declined to fully respond to his initial requests.

The Labor Department's interference with Chairman Johnson's request to the SEC was inappropriate and is indicative of the Department's overall posture in responding to the Chairman's inquiry into the rulemaking.<sup>220</sup> The Chairman had made a separate request to the SEC for documents in the possession and control of the SEC—a request for which the

<sup>216</sup> Email from Committee Staff, HSGAC, to Adri Jayaratne, Acting Asst. Sec'y, Office of Cong. & Intergovernmental Affairs, DOL (July 8, 2015, 6:56 PM) (on file with Committee).

<sup>217</sup> See Congressional Review Act, 5 U.S.C. §§ 801-808 (2012).

<sup>218</sup> Appendix A, Ex. 5, Letter from Chairman Johnson to Chairwoman White, SEC (July 13, 2015) ("If the Commission fails to immediately provide the requested documents, the Committee may consider use of the compulsory process.").

<sup>219</sup> Appendix A, Ex. 14, Letter from Acting Asst. Sec'y Jayaratne, DOL, to Chairman Johnson (July 8, 2015).

<sup>220</sup> Email from Committee Staff, HSGAC, to Adri Jayaratne, Acting Asst. Sec'y, Office of Cong. & Intergovernmental Affairs, DOL (July 8, 2015, 6:56 PM) (on file with Committee).



Department had no standing to interfere.<sup>221</sup> For reasons unknown to the majority staff, the Labor Department was unwilling to produce—and went out of its way to attempt to prevent others from producing—documents to the Committee about its work on this important rulemaking.

**c. OIRA Declined to Provide a Full and Complete Response to Chairman Johnson's Requests**

Chairman Johnson wrote a letter to OIRA on May 1, 2015, requesting information and documents relating to OIRA's review of the Labor Department's proposal.<sup>222</sup> After OIRA failed to provide a complete response, Chairman Johnson again wrote to OIRA on December 3, 2015.<sup>223</sup> To date, OIRA has provided non-specific, cursory responses to the Chairman's requests for information and produced limited materials that do not fully satisfy the Chairman's request for documents.<sup>224</sup>

Chairman Johnson's request stemmed from concern about whether OIRA conducted a thorough and thoughtful review of the rule. OIRA expedited its review, as evidence by the fact that the Labor Department promulgated the proposed rule just fifty days after OIRA received the proposal for review.<sup>225</sup> Chairman Johnson sought to ensure that OIRA conducted a thorough and thoughtful review of the proposed rule and to understand how OIRA incorporated suggestions from other Executive Branch departments and agencies and from stakeholders.<sup>226</sup> Specifically, Chairman Johnson asked OIRA to provide the following information:

1. Please provide all drafts of the Labor Department's proposed rulemaking, *including comments and suggestions to the drafts*.
2. Please explain why OIRA required considerably less time to review the Labor Department's proposed rulemaking than the average review time for other Labor Department regulatory proposals and other economically significant rules.
3. Please explain how OIRA incorporates suggestions from other Executive Branch departments and agencies, as well as stakeholders, into its review of the Labor Department's proposed rulemaking.
4. Please explain how the version of the proposed rulemaking incorporated OIRA's suggestions.

<sup>221</sup> *Id.*

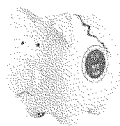
<sup>222</sup> Appendix A, Ex. 7, Letter from Chairman Johnson to Admin'r Shelanski, OIRA (May 1, 2015).

<sup>223</sup> Appendix A, Ex. 8, Letter from Chairman Johnson to Admin'r Shelanski, OIRA (Dec. 3, 2015).

<sup>224</sup> Appendix A, Ex. 18, Letter from Admin'r Shelanski, OIRA, to Chairman Johnson (Jan. 20, 2016).

<sup>225</sup> Appendix A, Ex. 7, Letter from Chairman Johnson to Admin'r Shelanski, OIRA (May 1, 2015).

<sup>226</sup> *Id.*



5. Please explain how OIRA evaluated the Labor Department's proposed rulemaking with respect to Executive Order 13563's requirements for coordination with other agencies and consideration of flexible approaches.

OIRA's May 18, 2015 response to the Chairman provided general information about OIRA's review process that was not specific to OIRA's review of the Labor Department's proposal.<sup>227</sup> Regarding its review of the Labor Department's proposal, OIRA provided only vague information:

OIRA devoted the time and resources necessary to ensure the review was consistent with EOs 12866 and 13563. This review included the participation of a number of relevant Executive Branch agencies. OIRA then concluded review of this draft on April 14, 2015. As background, EO 12866 provides OIRA up to 90 days to review significant regulatory actions, though the agency can request an extension. The amount of time needed to complete review on any given rule can vary, but OIRA does endeavor to complete the process as quickly as feasible while ensuring proper review.<sup>228</sup>

This answer lacked any specific information about the review process that Chairman Johnson requested.

OIRA's January 20, 2016 letter similarly lacked the specific information that Chairman Johnson requested.<sup>229</sup> OIRA simply stated:

Regarding the length of time the draft proposed rule was under review, I can assure you that OIRA devoted the time and resources necessary to ensure the review was in accordance with EOs 12866 and 13563. The amount of time needed to complete review on any given rule varies, but OIRA endeavors to complete the process as efficiently as possible while ensuring proper review. The review of the *Conflict of Interest* draft proposed rule included the participation of relevant Federal agencies.<sup>230</sup>

Again, this response contains a conclusory statement void of any specific information about OIRA's review of the Labor Department's rule. OIRA's document production also failed to satisfy Chairman Johnson's request.<sup>231</sup> OIRA provided drafts of the proposal, but the drafts do not contain comments or suggestions, which Chairman Johnson had

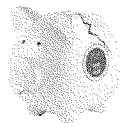
<sup>227</sup> Appendix A, Ex. 17, Letter from Admin'r Shelanski, OIRA, to Chairman Johnson (May 18, 2015).

<sup>228</sup> *Id.*

<sup>229</sup> Appendix A, Ex. 18, Letter from Admin'r Shelanski, OIRA to Chairman Johnson (Jan. 20, 2016).

<sup>230</sup> *Id.*

<sup>231</sup> *Id.* (document production on file with Committee).





requested.<sup>232</sup> OIRA also provided a list of meetings it took with members of the public related to the rule, and the materials provided to OIRA at the meetings.<sup>233</sup> The information and productions and that OIRA provided to the Committee fail to offer any insight into OIRA's review of the Labor Department's proposal.

## VI. CONCLUSION

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Chairman Johnson's inquiry into the Labor Department's proposed rule has revealed that the Labor Department prioritized an expedited rulemaking process at the expense of thoughtfully considering and incorporating advice and suggestions from industry experts. Additionally, career, non-partisan, professional staff at the SEC, career, non-partisan, regulatory experts at OIRA, and Treasury Department officials expressed concerns to the Labor Department about the rule. Yet, documents that the Committee received indicate that the Department failed to implement numerous recommendations from these government officials in other agencies.

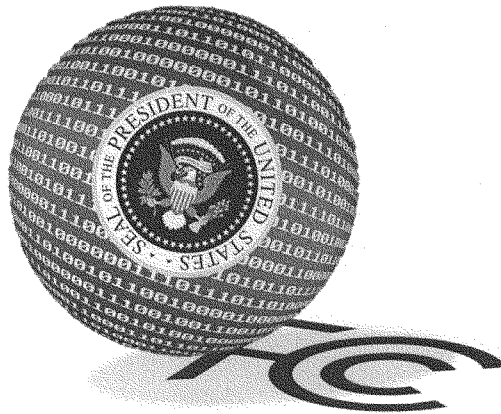
Chairman Johnson also encountered opposition and noncooperation from the Labor Department throughout its examination of the rulemaking process, calling into question the Department's commitment to transparency and accountability to Congress. From the information that the Committee was able to uncover, the Labor Department's flawed process in issuing its proposed "Conflict of Interest" rule could ultimately hurt American retirement savers. Whether intentionally or not, the proposed rule threatens to restrict access to retirement advice for those Americans who need it the most.

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<sup>232</sup> *Id.*

<sup>233</sup> *Id.*





**REGULATING THE INTERNET:  
HOW THE WHITE HOUSE BOWLED OVER FCC INDEPENDENCE**

A Majority Staff Report of the  
Committee on Homeland Security and Governmental Affairs  
United States Senate  
Senator Ron Johnson, Chairman



February 29, 2016

## EXECUTIVE SUMMARY

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The Federal Communications Commission (FCC or Commission) is an independent federal agency charged with regulating interstate and international communications. Deriving its regulatory authority from Congress, the agency is governed by five presidentially appointed Commissioners from both political parties. This bipartisan structure is intended to ensure that the agency remains free of partisan political pressure, and independent of the policy aims of the Executive Branch. Yet, according to a media report in February 2015, the Obama Administration sought to impose its will on the FCC's so-called Open Internet (OI) proposal. As detailed below, after the Obama White House weighed in, the FCC changed course and executed the President's preference.

On February 4, 2015, FCC Chairman Tom Wheeler announced a plan to reclassify broadband as a telecommunications service subject to Title II of the Communications Act of 1934 (47 U.S.C. 201 et. seq.). This announcement represented a shift from the FCC's previous light-touch approach of classifying broadband as an information service, and Chairman Wheeler's own statement in February 2014 that the FCC would use a roadmap outlined by the U.S. Court of Appeals for the D.C. Circuit (D.C. Circuit) in the court's ruling in *Verizon v. FCC* (740 F.3d 623 (2014)) that did not involve the reclassification of broadband as a common carrier service.<sup>1</sup> Concurrent with Chairman Wheeler's announcement, the *Wall Street Journal* reported that the White House may have inappropriately influenced the FCC decision to regulate broadband under Title II.<sup>2</sup> Specifically, the *Journal* noted "unusual, secretive efforts inside the White House, led by two aides."<sup>3</sup> Notably, in November 2014, President Obama had weighed in on the debate, imploring the FCC to "reclassify consumer broadband service under Title II ..."<sup>4</sup>

On February 9, 2015, Senator Ron Johnson, Chairman of the Senate Committee on Homeland Security and Government Affairs and a senior member of the Senate Committee on Commerce, Science and Transportation, initiated an inquiry into the FCC's OI Order in light of the information reported by the *Journal*.<sup>5</sup> In response to the Chairman's request, the FCC produced documents over the span of ten months and provided a staff briefing with key FCC staff members involved in the rulemaking. Nonetheless, the FCC withheld drafts of the OI proposal, including the draft that the FCC was in the process of finalizing just prior to the

<sup>1</sup> FED. COMM'NS COMM'N, Statement by FCC Chairman Tom Wheeler on the FCC's Open Internet Rules (Feb. 19, 2014), available at <https://www.fcc.gov/document/statement-fcc-chairman-tom-wheeler-fccs-open-internet-rules>.

<sup>2</sup> Gautham Nagesh & Brody Mullins, *How White House Thwarted FCC Chief on Internet Rules*, WALL ST. J., Feb. 4, 2015.

<sup>3</sup> *Id.*

<sup>4</sup> WHITE HOUSE, November 2014 The President's message on net neutrality, <https://www.whitehouse.gov/net-neutrality> (last visited Feb. 22, 2016).

<sup>5</sup> Appendix C, Ex. 1, Letter from Ron Johnson, Chairman, S. Comm. on Homeland Sec. & Gov't Affairs, to Tom Wheeler, Chairman, Fed. Commc'ns Comm'n (Feb. 9, 2015).



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President's statement. By withholding these key drafts, the FCC unnecessarily slowed and burdened the Committee's fact-finding regarding the process by which the FCC adopted its OI Order.

The investigation initiated by Chairman Johnson uncovered serious concerns with the President's undue influence on the FCC's decision-making process,<sup>6</sup> and also with the agency's compliance with the Administrative Procedure Act (APA). Specifically, the investigation found:

- Although President Obama's statement was filed in the FCC's record along with millions of other commenters, its influence was disproportionate relative to the comments of members of the public.<sup>7</sup> Prior to the White House's announcement, the career, nonpartisan, professional staff at the FCC worked over the weekend to deliver Chairman Wheeler an OI draft order to be considered on the FCC's December 2014 Open Meeting.<sup>8</sup> Immediately after the President's statement, FCC staff expressed confusion as edits were suddenly delayed and the rapid timetable of completing the draft OI Order was "paused."<sup>9</sup> At the conclusion of the pause, Chairman Wheeler instructed FCC staff to change course and draft an order that would follow the President's proposal of a Title II reclassification.<sup>10</sup>
- The FCC staff raised concerns about the agency following proper notice-and-comment procedure, as required under the APA.<sup>11</sup> Specifically, the FCC's career professional staff advised that the record to support Title II reclassification for both fixed and wireless

<sup>6</sup> As detailed below, while the President may lobby the FCC in favor of a certain policy outcome, the Justice Department cautions the White House to avoid the appearance of influence. *See infra* note 17. From the timeline presented in this report, a reasonable person could conclude that the FCC would not have ultimately chosen a Title II reclassification but for the President's support. *See BLACK'S LAW DICTIONARY* (10th ed. 2014) (defining "undue influence" as "The improper use of power or trust in a way that deprives a person of free will and substitutes another's objective; *the exercise of enough control over another person that a questioned act by this person would not have otherwise been performed, the person's free agency having been overmastered.*" (emphasis added)).

<sup>7</sup> E-mail from Stephanie Weiner, Fed. Commc'ns Comm'n, to Nese Guendelsberger, Fed. Commc'ns Comm'n & Matthew DelNero, Fed. Commc'ns Comm'n (Nov. 17, 2014) (describing the president's announcement as "a significant development") (HSGAC-OI-000149).

<sup>8</sup> E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Kristine Fargotstein, Fed. Commc'ns Comm'n (Nov. 7, 2014) (HSGAC-OI-032662) ("We're still going to try to get something to OCH on Monday, but folks understand that we can't address everything if we just get edits Monday morning.").

<sup>9</sup> *See e.g.*, E-mail from Paula Blizzard, Fed. Commc'ns Comm'n, to Travis LeBlanc et al., Fed. Commc'ns Comm'n (Nov. 10, 2014) (considering how the President's statement would impact the OI draft) (HSGAC-OI-002796); E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Thomas Parisi, Fed. Commc'ns Comm'n (Nov. 10, 2014, 9:48AM) (HSGAC-OI-000220);

<sup>10</sup> Briefing by Fed. Commc'ns Comm'n staff with S. Comm. on Homeland Sec. & Gov't Affairs staff (June 29, 2015).

<sup>11</sup> This issue is currently before the U.S. Court of Appeals for the District of Columbia Circuit in *United States Telecom Association v. FCC*, No. 15-1063 (D.C. Cir.).



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broadband was thin and needed to be bolstered.<sup>12</sup> Despite this recommend action, the FCC chose not to seek additional public comment, and proceeded with the President's proposal.

- A draft of the Open Internet Public Notice (PN) dated November 17, 2014, outlined *nine* issue areas of concern.<sup>13</sup> Yet, by November 19, it appears that the FCC's plan to seek further comment changed. Again, career professional staff expressed confusion in this redirection and a media aide pointed out to her colleagues: "NEED MORE ON WHY WE NO LONGER THINK RECORD IS THIN IN SOME PLACES."<sup>14</sup>
- To justify the FCC's sudden change in direction and to "beef up the record," FCC staff were asked if "additional comments filed since early November [2014] address some of the outstanding questions, i.e., mobile and forbearance?"<sup>15</sup> FCC staff were unable to establish an adequate basis to argue that recent public comments provided a sufficient justification for the Chairman's shifting approach.<sup>16</sup> To fill this void, General Counsel Jonathan Sallet solicited meetings with certain outside groups to support a rulemaking process for Title II reclassification.
- Over the course of the Committee's investigation, the FCC refused to provide key responsive documents. Moreover, in the emails that were provided to the Committee, it

<sup>12</sup> While the FCC's OI Notice of Proposed Rulemaking did pose a question "on the nature and the extent of the Commission's authority to adopt our open Internet rules relying on Title II, and other possible sources of authority, including Title III," it tentatively concluded "that the Commission exercise its authority under section 706, consistent with the D.C. Circuit's opinion in *Verizon v. FCC*, to adopt our proposed rules." Protecting and Promoting the Open Internet, 79 Fed. Reg. 37448, 37467 (May 15, 2014) (to be codified at 47 C.F.R. 8).

<sup>13</sup> E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Kristine Fargotstein, Fed. Commc'ns Comm'n (Nov. 17, 2014) (Listing issues for the draft public notice to include "classification/reclassification question", "edge service classification issue", "mobile classification issue (reclassify vs. hybrid)", "CMRS definition issue (reclassify vs. hybrid)", "broad forbearance paragraphs", "mobile-specific forbearance para/sentence", "mobile policy – transparency & RNM", "specialized services", "interconnection") (HSGAC-OI-032431-34).

<sup>14</sup> E-mail from Kim Hart, Fed. Commc'ns Comm'n, to Jonathan Sallet, Fed. Commc'ns Comm'n & Ruth Milkman, Fed. Commc'ns Comm'n (Nov. 21, 2014) (HSGAC-OI-18252-53).

<sup>15</sup> E-mail from Kim Hart, Fed. Commc'ns Comm'n, to Jonathan Sallet, Fed. Commc'ns Comm'n & Ruth Milkman, Fed. Commc'ns Comm'n (Dec. 1, 2014) (HSGAC-OI-18251-52).

<sup>16</sup> While the court will look to all of the comments submitted during the notice and comment period, the Majority staff found that FCC staff specifically searched for comments in the November 2014 time frame in order to justify why the record was no longer "thin"—Chairman Wheeler's initial explanation for the delay. *See e.g.*, E-mail from Kim Hart, Fed. Commc'ns Comm'n, to Jonathan Sallet, Fed. Commc'ns Comm'n & Ruth Milkman, Fed. Commc'ns Comm'n (Nov. 21, 2014) (HSGAC-OI-18252-53).



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appears that there was an attempt by some to thwart transparency and avoid *ex parte* filings.<sup>17</sup>

These issues, coupled with Chairman Wheeler's statements to the public and in Congressional testimony, raise real transparency and accountability issues. Specifically, Chairman Wheeler continues to assert "I was looking at a Title II and Section 706 approach before the President filed his position and we came out with a Title II, Section 706 approach."<sup>18</sup> If it were as simple as Chairman Wheeler implies, then it is logical to assume that the FCC would have voted on its OI Order in December, as the career, nonpartisan, professional staff at the FCC originally targeted (and worked weekends in order to meet). Instead, the FCC moved forward in a completely new direction months later—following the President's direction and apparently with concern from the career staff that there was insufficient notice to the public and affected stakeholders—with heavy-handed regulations on the broadband industry.

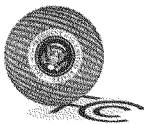
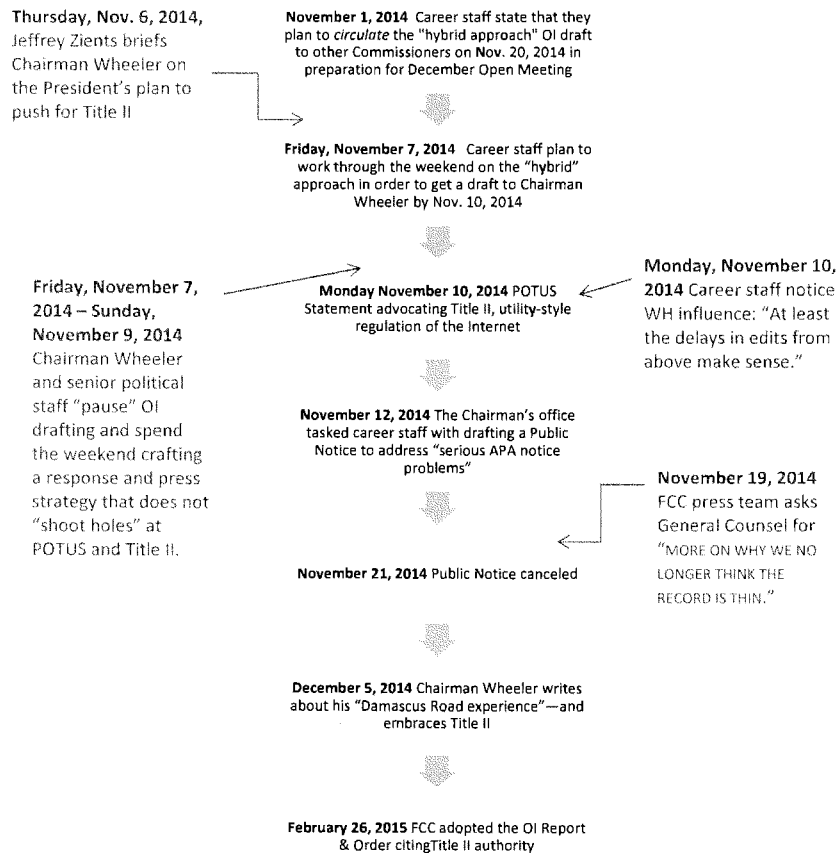
<sup>17</sup> *Ex Parte Communications During FCC Rulemaking*, 15 Op. O.L.C. 4 (1991) ("White House staff members should avoid even the mere appearance of interest or influence—and the easiest way to do so is to avoid discussing matters pending before the independent regulatory agencies with interested parties and avoid making *ex parte* contacts with agency personnel.") [hereinafter *O.L.C. Opinion*].

<sup>18</sup> *Oversight of the Federal Communications Commission: Hearing Before the S. Commerce, Sci., and Transp. Comm.*, 114th Cong. (2015).



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# OPEN INTERNET ORDER TIMELINE



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## I. INTRODUCTION

The FCC has been grappling with the issue of “net neutrality” for more than a decade. In 2005, the FCC adopted a policy statement that consumers were entitled to access their choice of legal Internet content; use services and run applications of their choosing; and have competition among network, application, service and content providers.<sup>19</sup> In April 2010, after the FCC had tried in 2008 to enforce an alleged violation of this policy statement against a company, its efforts were struck down by the D.C. Circuit in *Comcast v. FCC*.<sup>20</sup>

Despite any evidence of a problem, the FCC spent the rest of 2010 working towards an order that would impose affirmative rules on broadband providers. In December 2010, the FCC adopted, on a party-line 3-2 vote, its “Open Internet Order.”<sup>21</sup> In the 2010 order, the FCC carefully weighed whether or not to classify broadband services under Title II of the Communications Act. Title II regulations were crafted in the 1930s and designed to regulate “common carriers” or “public utilities.”

In the order, the FCC applied a light touch regulatory framework for fixed services, recognized the technical and competitive differences of wireless, and did not touch interconnection agreements.<sup>22</sup> The order specifically required broadband providers to disclose their network management practices and barred them from blocking legal traffic on their networks.<sup>23</sup> The rules also prohibited fixed broadband providers from unreasonably discriminating against Internet traffic, but did not apply this prohibition to wireless broadband providers.<sup>24</sup> Importantly, the FCC did not reclassify broadband as a Title II telecommunications service.

The new rules were challenged in court. On January 14, 2014, the D.C. Circuit upheld the FCC’s transparency rule but struck down the portions of the 2010 order that barred broadband providers from blocking content or unreasonable discrimination on their networks.<sup>25</sup> The court reasoned that the FCC had chosen not to classify broadband providers as common carriers, and therefore could not impose common carrier obligations. At the same time, the court provided the FCC with a roadmap on how to impose rules on broadband providers that would address the type of conduct about which the FCC was purportedly concerned without subjecting

<sup>19</sup> Fed. Commc’ns Comm’n, New Principles Preserve and Promote the Open and Interconnected Nature of Public Internet (Aug. 5, 2005).

<sup>20</sup> 600 F.3d 642 (D.C. Cir. 2010).

<sup>21</sup> Fed. Commc’ns Comm’n, Report and Order, In re: Preserving the Open Internet Broadband Industry Practices (Dec. 21, 2010).

<sup>22</sup> *Id.*

<sup>23</sup> *Id.*

<sup>24</sup> *Id.*

<sup>25</sup> *Verizon v. Fed. Commc’ns Comm’n*, 740 F.3d 623 (D.C. Cir. 2014).



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such providers to common carrier requirements. FCC Chairman Tom Wheeler appeared to accept this direction, and in February 2014 announced that the FCC would pursue a new rulemaking based on this roadmap.<sup>26</sup> Specifically, Chairman Wheeler proposed that broadband providers could charge companies different prices for different services on their networks provided that such deals were “commercially reasonable.”<sup>27</sup> On May 15, 2014 the FCC issued a Notice of Proposed Rulemaking (NPRM) that largely reflected the Chairman’s earlier proposal.<sup>28</sup>

By the end of 2014, it became widely reported that the FCC would move forward on a Final Order adopting a “hybrid approach.”<sup>29</sup> The hybrid approach divided the Internet into “wholesale” and “retail” transactions. Wholesale transactions, or transactions conducted on the “back-end” of the Internet between the content provider and Internet service provider, would be regulated as a public utility. Meanwhile, retail transactions, or the transaction sending data from the Internet service provider to the consumer, would receive a lighter regulatory touch.<sup>30</sup>

The same week the FCC was preparing to circulate a draft proposal on the hybrid approach, the President directly weighed into the debate, stating: “I believe the FCC should reclassify consumer broadband service under Title II of the Telecommunications Act.”<sup>31</sup> On February 4, 2015, Chairman Wheeler revealed his plan to regulate broadband as a Title II utility service, treat wireless the same as fixed broadband, and assert jurisdiction over Internet interconnection agreements for the first time.<sup>32</sup> Not only did this plan constitute a monumental shift from the 2010 FCC order, but it also represented a very large deviation from Chairman

<sup>26</sup> FED. COMM’NS COMM’N, Statement by FCC Chairman Tom Wheeler on the FCC’s Open Internet Rules (Feb. 19, 2014), available at <https://www.fcc.gov/document/statement-fcc-chairman-tom-wheeler-fccs-open-internet-rules>; see also *Oversight of the Federal Communications Commission: Hearing Before the S. Comm. on Commerce, Sci., and Transp.*, 114th Cong. (2015).

<sup>27</sup> See e.g., Fed. Commc’ns Comm’n, Notice of Proposed Rulemaking, In re: Preserving and Promoting the Open Internet (May 15, 2014) (describing broadband providers ability to “serve customers and carry traffic on an individually negotiated basis” to be commercially reasonable).

<sup>28</sup> Fed. Commc’ns Comm’n, Notice of Proposed Rulemaking, In re: Preserving and Promoting the Open Internet (May 15, 2014).

<sup>29</sup> See e.g., Gautham Nagesh, *FCC ‘Net Neutrality’ Plan Calls for More Power Over Broadband*, WALL ST. J., Oct. 30, 2014; Edward Wyatt, *F.C.C. Considering Hybrid Regulatory Approach to Net Neutrality*, N.Y. TIMES, Oct. 31, 2014.

<sup>30</sup> See E-mail from Tom Wheeler, Chairman, Fed. Commc’ns Comm’n, to Ruth Milkman et al., Fed. Commc’ns Comm’n (Dec. 5, 2014) (describing the hybrid approach) (HSGAC-OI-031391-97).

<sup>31</sup> WHITE HOUSE, November 2014 The President’s message on net neutrality, <https://www.whitehouse.gov/net-neutrality> (last visited Feb. 22, 2016). Please note that Title II of the Telecommunications Act of 1996 actually deals with broadcast services, but that the President clearly intended to refer to Title II of the Communications Act, which covers common carriers.

<sup>32</sup> See FED. COMM’NS COMM’N, *Fact Sheet: Chairman Wheeler Proposes New Rules for Protecting the Open Internet* (Feb. 4, 2015), available at [https://apps.fcc.gov/edocs\\_public/attachmatch/DOC-331869A1.pdf](https://apps.fcc.gov/edocs_public/attachmatch/DOC-331869A1.pdf); see also Tom Wheeler, *This is how we will ensure net neutrality*, WIRED, Feb. 4, 2015.



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Wheeler's original NPRM and the light regulatory touch that had been applied to broadband services since the Clinton Administration.

In an op-ed in *Wired* magazine, Chairman Wheeler explained that this evolution occurred because he became concerned that a commercial reasonableness standard might, down the road, be interpreted to mean what is reasonable for commercial interests, not consumers.<sup>33</sup> However, emails and information obtained by the Committee reveal that undue outside political pressure led the FCC to this decision. Documents produced to the Committee reveal concerns among FCC staff about potential APA violations stemming from Chairman Wheeler's shift to Title II regulation, as well as serious transparency failures from the FCC in terms of compliance with congressional oversight and *ex parte* requirements.<sup>34</sup>

## II. THE WHITE HOUSE EXERTED UNDUE INFLUENCE ON THE FCC'S OPEN INTERNET RULEMAKING

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Congress established the FCC as an independent agency with the mission of regulating interstate and international communications within, from, and to the United States. As an independent agency, the president's influence over the FCC, by design, should be limited.<sup>35</sup> For example, the president's power to remove officers is not the same with leaders of an independent agency as it is with subordinate executive branch officers. The President can only remove independent agency heads "for cause," meaning that they cannot be removed for political disagreements.<sup>36</sup> These statutory limits on the president's power over independent agencies—like the FCC—demonstrate the importance of maintaining the agency's independence.<sup>37</sup>

The documents provided to the Committee do not paint the same picture that Chairman Wheeler outlined in his February 2015 *Wired* op-ed. In contrast, these documents suggest that the White House exerted undue influence on the FCC's decision to abandon its hybrid approach and regulate broadband under Title II.

Emails show that the career, nonpartisan, professional staff at the FCC identified White House influence in the drafting process of the OI Order almost immediately after the President's

<sup>33</sup> Wheeler, *supra* note 24.

<sup>34</sup> See O.L.C. Opinion, *supra* note 16.

<sup>35</sup> In an executive agency, the President has many tools at his disposal to exert policymaking influence, one of which is the power to remove an executive officer at-will. See generally *Myers v. United States*, 272 U. S. 52 (1926).

<sup>36</sup> See *Humphrey's Executor v. United States*, 295 U. S. 602 (1935) (finding that the President's unrestrained removal power does not extend to heads of independent agencies).

<sup>37</sup> See e.g., *Humphrey's Executor*, 295 U. S. 602, 629 ("one who holds his office only during the pleasure of another cannot be depended upon to maintain an attitude of independence against the latter's will").



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public statement.<sup>38</sup> After President Obama came out in favor of Title II regulations, FCC career staff opined, “[n]ot sure how this will affect the current draft and schedule—but I suspect substantially . . . .”<sup>39</sup> In another instance, an FCC employee who was assisting in drafting the OI Order responded to a news alert about the President’s statement, writing “[t]his might explain our delay.”<sup>40</sup> The staff member, who spent her weekend working on the OI Order, separately wrote, “at least the delays in edits from above make sense . . . .”<sup>41</sup>

**Item 1: Email exchange between FCC employees (Nov. 10, 2014)**

**To:** Travis LeBlanc; Martha Heller; Stephen Ruckman; Gregory Simon; Christopher Killian; Rosemary McEnery  
**From:** Paula Blizzard  
**Sent:** Mon 11/10/2014 4:02:32 PM  
**Subject:** OI - Obama says make it title II

Chris and Rosemary just alerted me to breaking news - Obama says to make it Title II:

President Obama has come out in support of reclassifying internet service as a utility, a move that would allow the Federal Communications Commission to enforce more robust regulations and protect net neutrality. **"To put these protections in place, I'm asking the FCC to reclassifying internet service under Title II of a law known as the Telecommunications Act."** Obama says in a statement this morning. "In plain English, I'm asking [the FCC] to recognize that for most Americans, the internet has become an essential part of everyday communication and everyday life."

<http://www.theverge.com/2014/11/10/7185933/fcc-should-reclassify-internet-as-utility-obama-says>

Not sure how this will affect the current draft and schedule - but I suspect substantially . . . .

<sup>38</sup> E-mail from Paula Blizzard, Fed. Commc'ns Comm'n, to Travis LeBlanc et al., Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-002796); E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Thomas Parisi, Fed. Commc'ns Comm'n (Nov. 10, 2014, 9:48AM) (HSGAC-OI-000220); E-mail from Thomas Parisi, Fed. Commc'ns Comm'n, to Kristine Fargotstein, Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-007493); E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-032602); E-mail from Melissa Droller Kinkel, Fed. Commc'ns Comm'n, to Claude Aiken et al., Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-018630).

<sup>39</sup> E-mail from Paula Blizzard, Fed. Commc'ns Comm'n, to Travis LeBlanc et al., Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-002796).

<sup>40</sup> E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Thomas Parisi, Fed. Commc'ns Comm'n (Nov. 10, 2014, 9:48AM) (HSGAC-OI-000220).

<sup>41</sup> E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-032602); E-mail from Melissa Droller Kinkel, Fed. Commc'ns Comm'n, to Claude Aiken et al., Fed. Commc'ns Comm'n (Nov. 10, 2014) (HSGAC-OI-018630).



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## Item 2: Email exchange between FCC employees (Nov. 10, 2014)

**Thomas Parisi**

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**From:** Thomas Parisi  
**Sent:** Monday, November 10, 2014 9:49 AM  
**To:** Kristine Fargotstein  
**Subject:** RE: Technology Breaking News

It might indeed.

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**From:** Kristine Fargotstein  
**Sent:** Monday, November 10, 2014 9:48 AM  
**To:** Thomas Parisi  
**Subject:** RE: Technology Breaking News

Yes. This might explain our delay.

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**From:** Thomas Parisi  
**Sent:** Monday, November 10, 2014 9:48 AM  
**To:** Kristine Fargotstein  
**Subject:** RE: Technology Breaking News

Did you mean to send it just to me? But yeah that was interesting. Politico pro breaking news alerts are the best!

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**From:** Kristine Fargotstein  
**Sent:** Monday, November 10, 2014 9:46 AM  
**To:** Thomas Parisi  
**Subject:** FW: Technology Breaking News

FYI

---

**From:** POLITICO Pro [mailto:politicopro@mail.politicopro.com]  
**Sent:** Monday, November 10, 2014 9:39 AM  
**To:** Kristine Fargotstein  
**Subject:** Technology Breaking News

President Barack Obama waded directly into the debate over net neutrality today, calling for stronger regulation of open Internet rules.



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**Item 3: Email exchange between FCC employees (Nov. 10, 2014)**

**From:** Kristine Fargotstein [REDACTED]  
**Sent:** 11/10/2014 1:50:10 PM  
**To:** Claude Aiken [REDACTED]  
**Subject:** RE: FCC Daily News Briefing for Monday, November 10, 2014

At least the delays in edits from above now makes sense...

**From:** Claude Aiken  
**Sent:** Monday, November 10, 2014 8:50 AM  
**To:** Melissa Droller Kinkel; Kristine Fargotstein; Thomas Parisi; Zachary Ross  
**Subject:** RE: FCC Daily News Briefing for Monday, November 10, 2014

I saw. Will try to get to the bottom of this this morning.

\*\*\* Non-Public: For Internal Use Only \*\*\*

-----Original Message-----

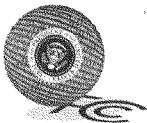
**From:** Melissa Droller Kinkel  
**Sent:** Monday, November 10, 2014 07:57 AM Eastern Standard Time  
**To:** Claude Aiken; Kristine Fargotstein; Thomas Parisi; Zachary Ross  
**Subject:** FW: FCC Daily News Briefing for Monday, November 10, 2014

There is also an article about delaying the item in the Wall Street journal but I don't have access to the full article.

Confusion among the career professional staff at the FCC is not surprising after comparing the pace and momentum at which they were working before and after the President's statement on November 10, 2014. An email from Scott Jordan, the FCC's Chief Technology Officer, to Matt Del Nero, Chief of the Wireline Competition Bureau (Deputy Chief at the time in question) and Eric Feigenbaum, a staffer in Office of Media Relations, confirms that, as of November 1, 2014, there was a plan in place to circulate the OI Order on November 20, 2014.<sup>42</sup> According to FCC precedent and common practice, November 20 would have been the last day to circulate the OI Order to FCC commissioners in time for it to appear on the December 2014 Open Meeting agenda and also to stay in compliance with sunshine laws.<sup>43</sup>

<sup>42</sup> E-mail from Scott Jordan, Fed. Commc'ns Comm'n, to Matthew DelNero, Fed. Commc'ns Comm'n (Nov. 1, 2014) (HSGAC-OI-004977).

<sup>43</sup> See, Michael O'Rielly, Commissioner, Fed. Commc'ns Comm'n, *FCC's Pre-Adoption Process Also Needs Work*, FCC Blog (April 1, 2015, 12:55pm), available at <https://www.fcc.gov/news-events/blog/2015/04/01/fcc%E2%80%99s-pre-adoption-process-also-needs-work> ("Commissioners receive meeting items from staff, on behalf of the Chairman, not less than three weeks in advance of a Commission Agenda Meeting .... During the first two weeks, outside parties may meet with Commissioners and staff to advocate their views and seek changes, if necessary. The last week of the three-week period is the Sunshine period."); Government in the Sunshine Act, 5 U.S.C. § 552(b) (1976); 47 C.F.R. § 1.1203 (2016).



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As late as Sunday, November 9, career FCC staffers were working diligently to finalize a draft so that the OI Order could be considered by the commissioners at the FCC's Open Meeting scheduled for December 11, 2014. Between November 1 and November 7, professional staff worked on edits with a goal of having a full draft ready for Chairman Wheeler's review by November 10.<sup>44</sup> Emails exchanged among FCC career staff responsible for drafting portions of the OI Order between November 7 and 9 confirm that staff planned to and did work throughout the weekend prior to the President's statement in order to get a draft to "OCH [Office of the Chairman] on Monday."<sup>45</sup>

While career professional staff worked weekend shifts on the draft OI Order for Chairman Wheeler, senior staff at the FCC had already changed directions.<sup>46</sup> At a later hearing of the Senate Committee on Commerce, Science, and Transportation, Chairman Wheeler confirmed to Senator Johnson that he was briefed about the President's speech on Thursday, November 6, 2014 by Jeffrey Zients, Assistant to the President for Economic Policy.<sup>47</sup> During the weekend between Chairman Wheeler's briefing by Jeffrey Zients and the President's statement—the same weekend that career staff worked on the OI Order—the FCC media team and senior staff were focused on damage control. They crafted an internal "Q&A" document, with edits from Chairman Wheeler directly, in preparation for the anticipated media coverage of President Obama's statement.<sup>48</sup> In the Q&A document, FCC media staff posed an anticipated

<sup>44</sup> See E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Kristine Fargotstein, Fed. Commc'ns Comm'n (Nov. 7, 2014) (making clear that the goal over the next couple of days, including the weekend, is to get a draft to the Chairman by Monday, November 10) (HSGAC-OI-032662-63); see e.g., E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Aaron Garza et al., Fed. Commc'ns Comm'n (Nov. 6, 2014) (compiling sections of the OI draft and making style and grammar edits) (HSGAC-OI-032710-12).

<sup>45</sup> E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 7, 2014) (HSGAC-OI-032663) (making a chart of staff availability over the weekend); E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 8, 2014) (reviewing edits on Saturday (11/8) and Sunday (11/9) in order to make the Monday deadline) (HSGAC-OI-032657); E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Denise Coca, Fed. Commc'ns Comm'n (Nov. 8, 2014) (soliciting edits from other staff on Saturday afternoon (11/9)) (HSGAC-OI-032546).

<sup>46</sup> Documents show that General Counsel Jonathan Sallet, Chief of Staff Ruth Milkman, Senior Advisor Philip Verveer, and Media Relations Director Shannon Gilson—among others—were already pivoting away from the hybrid approach. Milkman, Verveer, and Sallet joined the FCC the same day Tom Wheeler became Chairman. See Press Release, Fed. Commc'ns Comm'n, FCC Chairman Tom Wheeler Announces Staff Appointments (Nov. 4, 2013), available at [https://apps.fcc.gov/edocs\\_public/attachmatch/DOC-323962A1.pdf](https://apps.fcc.gov/edocs_public/attachmatch/DOC-323962A1.pdf) (describing senior staff appointments by Chairman Wheeler).

<sup>47</sup> *Oversight of the Federal Communications Commission: Hearing Before the S. Commerce, Sci., and Transp. Comm.*, 114th Cong. (2015).

<sup>48</sup> E-mail from Tom Wheeler, Chairman, Fed. Commc'ns Comm'n, to Shannon Gilson, Director, Office of Media Relations, Fed. Commc'ns Comm'n, Jonathan Sallet, General Counsel, Fed. Commc'ns Comm'n, Philip Verveer, Senior Counsel to Chairman, Fed. Commc'ns Comm'n, & Ruth Milkman, Chief of Staff, to Chairman, Fed. Commc'ns Comm'n (Nov. 9, 2014) (rationalizing that Wheeler "did not know the specific substance of the President's letter until he read the public document") (HSGAC-OI-031304-07).



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question of whether there were discussions between the White House and the FCC leading up to the President's statement. In response to a proposed answer that "there have not been substantive discussions," the document drafter asked incredulously: "IS THIS RIGHT?"<sup>49</sup>

**Item 4: Q&A document prepared for Chairman Wheeler (Nov. 9, 2014)**

Q. Has there been discussions between the WH and the FCC leading up to this rollout?  
A. The FCC kept the WH apprised of the process thus far, but there have not been substantive discussions. (IS THIS RIGHT?)

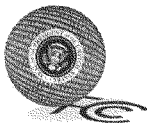
While Chairman Wheeler claims that "he did not know the specific substance of the President's letter" until Monday, November 10 when it was made public,<sup>50</sup> the editing process revealed deliberate efforts to avoid "shoot[ing] holes into POTUS'[s] proposal and taking a swing at Title II."<sup>51</sup> At a minimum, the weekend emails demonstrate that Chairman Wheeler was personally aware *prior* to the President's statement that the President would advocate for full Title II, utility-style regulation, which was presumably a topic of conversation at his November 6 meeting with Jeffrey Zients.<sup>52</sup>

<sup>49</sup> E-mail from Kim Hart, Press Secretary, Fed. Commc'ns Comm'n, to Tom Wheeler et al., Fed. Commc'ns Comm'n (Nov. 9, 2014) (HSGAC-OI-031064).

<sup>50</sup> E-mail from Tom Wheeler, Fed. Commc'ns Comm'n, to Shannon Gilson, et al., Fed. Commc'ns Comm'n (Nov. 9, 2014) ("Q: How did the Chairman find out about the POTUS' letter? A: The Chairman was informed Thursday evening in the broadest possible terms. He did not know the specific substance of the President's letter until he read the public document") (HSGAC-OI-031304-07); E-mail from Jonathan Sallet, Fed. Commc'ns Comm'n, to Tom Wheeler et al., Fed. Commc'ns Comm'n (Nov. 9, 2014) (editing Wheeler's response to the President's Nov. 10, 2014 statement in favor of regulating the Internet as a utility) (HSGAC-OI-031067-72).

<sup>51</sup> E-mail from Shannon Gilson, Fed. Commc'ns Comm'n, to Tom Wheeler, Fed. Commc'ns Comm'n (Nov. 9, 2014) (HSGAC-OI-031068).

<sup>52</sup> Compare E-mail from Kim Hart, Press Secretary, Fed. Commc'ns Comm'n, to Shannon Gilson, Fed. Commc'ns Comm'n (Nov. 9, 2014, 7:43PM) (Kim Hart drafting a press Q&A document including the following: "Q: The Chairman says he shares the same position as the President, but POTUS is calling for Title II and the Chairman has called for 706 and a hybrid approach. So how can they share the same position if they are calling for different legal solutions? A: The Chairman and the President share the same goals – keeping the Internet open as[a] platform for innovation, expression and economic growth. The Chairman has said all options are on the table and no final decision has been made.") (HSGAC-OI0031063-66) with E-mail from Tom Wheeler, Fed. Commc'ns Comm'n, to Shannon Gilson et al., Fed. Commc'ns Comm'n (Nov. 9, 2014, 9:17PM) (Tom Wheeler editing the Q&A document, including the following: "Q: The Chairman says he shares the same position as the President, but POTUS is calling for Title II and the Chairman has called for 706 and a hybrid approach. So how can they share the same position if they are calling for different legal solutions? A: The Chairman and the President share the same goals – keeping the Internet open as [a] platform for innovation, expression and economic growth. The Chairman has often said he is opposed to Internet fast lanes and to accomplish that all options are on the table and no final decision has been made.") (HSGAC-OI-031304-07).





It is also clear from documents obtained by the Committee that President Obama's advocacy for Title II prompted the FCC to immediately pull the OI Order from the December 2014 meeting agenda. In subsequent testimony, Chairman Wheeler admitted that the OI Order was scheduled for the December Opening meeting.<sup>53</sup> When asked for the reason of the delay, Chairman Wheeler stated "it was a bridge too far" and "you can whip the horse, but you can't make it go faster sometimes," and ultimately blaming "the staff" who "just couldn't get the work done."<sup>54</sup> Based on emails, however, the career FCC staff was prepared and on schedule, albeit by working on the weekends, to move forward with the OI Order at the December Open Meeting. The only impediment to getting the work done appears to be the White House's intervention.

In June 2015, Committee staff received a briefing about the process of drafting the OI Order from Roger Sherman, then Chief of the Wireless Telecommunications Bureau, and Matt DelNero, Chief of the Wireline Competition Bureau (Deputy Chief at the time in question).<sup>55</sup> They informed Committee staff that, in the fall of 2014, FCC career professional staff wrote a draft OI Order that utilized the hybrid approach.<sup>56</sup> FCC staff apparently prepared several drafts of the order, all of which incorporated the hybrid approach.<sup>57</sup> According to the briefing, Chairman Wheeler was aware of—and supported—this effort as late as October 2014.<sup>58</sup>

While it is true that the stock values of broadband providers did not crash immediately after the President's announcement, the FCC's OI Order has had a clear impact on the market. According to the Progressive Policy Institute, in the first half of 2015, capital expenditures by major Internet Service Providers (ISPs) dropped an average of 12 percent. (See L. Gordon Covitz, *Obamanet Is Hurting Broadband*, Wall St. J. (Sept. 13, 2015)). As Commissioner Pai testified to Chairman Johnson at a Senate Commerce Committee hearing, "You have to pay the piper when it comes to Title II. And the proof is going to be in the pudding in the months to come, not in the ephemeral stock variations." (*Oversight of the Federal Communications Commission: Hearing Before the S. Comm. on Commerce, Sci., and Transp.*, 114th Cong. (2015)).

Mr. Sherman and Mr. DelNero confirmed that there was a "pause" of a few weeks after Chairman Wheeler met with Mr. Zients on November 6th so that the FCC could reconsider the merits of its hybrid approach and assess how the President's announcement affected the

<sup>53</sup> FCC: *Process and Transparency: Hearing Before the H. Comm. on Oversight and Gov't Reform*, 114th Cong. (2015).

<sup>54</sup> *Id.*

<sup>55</sup> Briefing provided by Fed. Comm'n's Comm'n staff for Comm. on Homeland Sec. & Gov't Affairs staff (June 29, 2015).

<sup>56</sup> *Id.*

<sup>57</sup> *Id.*

<sup>58</sup> *Id.*



market.<sup>59</sup> During this time, career professional staff working on the OI Order also recognized that the “Open Internet is on pause.”<sup>60</sup> On November 21, 2014, Jonathan Sallet, FCC General Counsel, began drafting written testimony for Chairman Wheeler regarding the OI Order.<sup>61</sup> The draft testimony pointed to “the aftermath of the President’s statement”—stability in the markets after the announcement—as “convincing proof that the application of Title II need not deter future investment.”<sup>62</sup> With this justification in mind, at the conclusion of the few week “pause,” Chairman Wheeler instructed FCC staff to follow a pure Title II reclassification.<sup>63</sup>

Chairman Wheeler in Congressional hearings and in public statements denies that the White House dictated the agency’s decision on net neutrality. When questioned by Chairman Johnson in April 2015, Chairman Wheeler stated: “I was looking at a Title II and Section 706 approach before the President filed his position and we came out with a Title II, Section 706 approach.” However, if it were that simple, it strains credulity to believe that Chairman Wheeler was unable to “whip the horse” (that is, the FCC’s professional career staff) to get the OI Order on the December meeting agenda as planned.<sup>64</sup> This is particularly puzzling when it is clear that professional career staff worked weekends to stay on track and deliver Chairman Wheeler’s original proposal in a timely manner.

A review of the documents provided to the Committee demonstrates that the FCC was actively drafting an OI Order using the hybrid approach prior to President Obama’s November 10, 2014 statement in favor of Title II, utility-style regulation. It is clear that once Chairman Wheeler was aware of the President’s imminent statement, Chairman Wheeler and senior staff “paused” drafting the OI Order even though career, professional staff were prepared and willing to get the draft finished. When the “pause” was over, Chairman Wheeler directed staff to draft an OI Order embracing Title II. Chairman Wheeler even alluded to the White House’s influence on the rulemaking during a speech at the Federal

“The FCC has approved President Obama’s plan to ensure a free and open internet.” - Email from the Democratic National Committee, February 27 2015. (*Oversight of the Federal Communications Commission: Hearing Before the S. Comm. on Commerce, Sci., and Transp.*, 114th Cong. (2015)).

<sup>59</sup> *Id.*

<sup>60</sup> E-mail from Claude Aiken, Fed. Commc’ns Comm’n, to Alexis Johns, Fed. Commc’ns Comm’n (Nov. 10, 2014, 2:35PM) (HSGAC-OI-009105).

<sup>61</sup> E-mail from Jonathan Sallet, Fed. Commc’ns Comm’n, to Philip Verveer, Senior Counsel to the Chairman, Fed. Commc’ns Comm’n (Nov. 21, 2014) (HSGAC-OI-018370).

<sup>62</sup> *Id.*

<sup>63</sup> Briefing provided by Fed. Commc’ns Comm’n staff for Comm. on Homeland Sec. & Gov’t Affairs staff (June 29, 2015).

<sup>64</sup> *Oversight of the Federal Communications Commission: Hearing Before the S. Commerce, Sci., and Transp. Comm.*, 114th Cong. (Mar. 2015).



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Communications Bar Association's "Chairman Dinner," where he joked, "I would like to thank Mozilla Foundation for the first draft of my remarks tonight, and President Obama for his edits."<sup>65</sup> His jest had more than a kernel of truth to it: FCC staff was actively preparing a hybrid draft order up until the President's announcement in favor of Title II.

### III. FCC STAFF RECOGNIZED DEFICIENCIES IN THE RECORD AND WORRIED ABOUT POTENTIAL VIOLATIONS OF THE ADMINISTRATIVE PROCEDURE ACT

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Following the President's statement on November 10 urging the FCC to regulate broadband under Title II, the FCC shifted to a Title II approach. In doing so, however, documents show that career FCC staff worried that the sudden change would violate federal law governing agency rulemaking.<sup>66</sup> In particular, the APA requires federal agencies to provide for "notice and comment" of proposed action.<sup>67</sup> Here, due to swift change in course, FCC career staff worried that the agency could be violating federal law.

Under the APA, an agency is authorized to promulgate rules through a notice-and-comment process.<sup>68</sup> Because final agency orders are binding, proposals that go through notice-and-comment rulemaking are designed to give stakeholders and the public the opportunity to weigh in on how proposed rules would affect their interests. Typically, the agency proposes a rule, stakeholders and the public comment, and the agency considers those comments as it drafts a final rule. The process is not supposed to serve as a means for an agency to justify a predetermined outcome.<sup>69</sup> Courts have invalidated agency rules for not allowing the public sufficient opportunity to comment.<sup>70</sup>

Only two days into the "pause" period that resulted from the President's statement on net neutrality, Chairman Wheeler's office directed career professional staff at the FCC to identify

<sup>65</sup> Brooks Boliek et al., *The FCC chair's Internet pivot*, POLITICO (Feb. 2, 2015, 5:36 AM), <http://www.politico.com/story/2015/02/tom-wheeler-net-neutrality-114785>.

<sup>66</sup> See e.g., E-mail from Matthew DeNero, Fed. Commc'ns Comm'n, to Jim Schlichting, Fed. Commc'ns Comm'n (identifying the application of Title II to mobile and the redefinition of CMRS as "a serious APA notice problem") (HSGAC-OI-032539).

<sup>67</sup> Administrative Procedure Act (APA), 5 U.S.C. §553 (1946).

<sup>68</sup> Administrative Procedure Act (APA), 5 U.S.C. §551 et seq. (1946).

<sup>69</sup> See *HBO, Inc. v. FCC*, 567 F.2d 9, 35-36 (D.C. Cir. 1977) (finding that the agency must provide notice to the public before the final rule is adopted or the opportunity to comment is meaningless).

<sup>70</sup> See *Allina Health Servs. v. Sebelius*, 746 F.3d 1102, 1110-11 (D.C. Cir. 2014) (vacating a rule because it was not a logical outgrowth and the agency "did not provide adequate notice and opportunity to comment").



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issues that would be covered in a Further Notice of Proposed Rulemaking (FNPRM), sometimes referred to as a Public Notice (PN).<sup>71</sup> The issues were to be separated into three buckets:

1. “areas where there is a *serious APA notice problem* with substantial litigation risk,”
2. “areas where we could expect to *have to argue that our actions were a logical outgrowth* of the NPRM,” and
3. “areas we are confident that we have adequate notice but would be better informed by more targeted comment.”<sup>72</sup>

Responses poured in from FCC staff working on the OI Order.<sup>73</sup> One career professional staffer in the Wireline Competition Bureau suggested “[w]e would want to seek further comment on changing the definition of ‘public switched network,’ including proposing a revised definition that would expand the term to refer to broadband Internet access networks.”<sup>74</sup> Scott Jordan, Chief Technology Officer, wrote to General Counsel Jonathan Sallet warning that “[r]egarding discriminatory practices, refusals to upgrade capacity, and access fees, *the notice is fairly poor*, consisting mainly of a single general question.”<sup>75</sup> With respect to forbearance—the process of determining which provisions of Title II would not apply—Mr. DelNero identified “forbearance for mobile generally” and “forbearance for re/classification of a service that reaches interconnection” as issues which “likely need more comment in the record.”<sup>76</sup>

A draft of the Open Internet PN dated November 17, 2014, outlined *nine* issue areas of concern.<sup>77</sup> Career professional staff compiled this draft for review by Roger Sherman and Julie

<sup>71</sup> See e.g., E-mail from Matthew DelNero, Fed. Commc’ns Comm’n, to Jim Schlichting, Fed. Commc’ns Comm’n & Joel Taubenblatt, Fed. Commc’ns Comm’n (Nov. 12, 2014) (making clear that the request for FNPRM topics was coming from “OCH”) (HSGAC-OI-008311).

<sup>72</sup> E-mail from Matthew DelNero, Fed. Commc’ns Comm’n, to Jim Schlichting, Fed. Commc’ns Comm’n (putting the application of Title II to mobile and the redefinition of CMRS in the category of “a serious APA notice problem”) (HSGAC-OI-032539).

<sup>73</sup> See e.g., E-mail from Scott Jordan, Fed. Commc’ns Comm’n, to Jonathan Sallet, Fed. Commc’ns Comm’n (Nov. 12, 2014) (analyzing gaps in the OI proceeding by comparing the notice and the record) (HSGAC-OI-024547).

<sup>74</sup> E-mail from Jennifer Salhus, Fed. Commc’ns Comm’n, to Joel Taubenblatt, Fed. Commc’ns Comm’n (Nov. 12, 2014) (HSGAC-OI-028347).

<sup>75</sup> E-mail from Scott Jordan, Fed. Commc’ns Comm’n, to Jonathan Sallet, Fed. Commc’ns Comm’n (Nov. 13, 2014) (HSGAC-OI-037046 (emphasis added)).

<sup>76</sup> E-mail from Matthew DelNero, Fed. Commc’ns Comm’n, to Jonathan Sallet, Fed. Commc’ns Comm’n (Nov. 12, 2014) (HSGAC-OI-008312); see also Email from Thomas Parisi, Fed. Commc’ns Comm’n, to Melissa Droller Kinkel, Fed. Commc’ns Comm’n (Nov. 14, 2014) (HSGAC-OI-032465-66).

<sup>77</sup> E-mail from Claude Aiken, Fed. Commc’ns Comm’n, to Kristine Fargotstein, Fed. Commc’ns Comm’n (Nov. 17, 2014) (drafting a Public Notice to seek additional comment on “classification/reclassification question”, “edge service classification issue”, “mobile classification issue (reclassify vs. hybrid)”, “CMRS definition issue (reclassify vs. hybrid)”, “broad forbearance paragraphs”, “mobile-specific forbearance para/sentence”, “mobile policy – transparency & RNM”, “specialized services”, “interconnection”) (HSGAC-OI-032431-34).



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Veach, former Wireline Competition Bureau Chief.<sup>78</sup> Under FCC drafting procedures, after review by the Bureau Chiefs, the document was sent to the Chairman's office.<sup>79</sup> Career professional staff began preparations to release the PN to the federal register on November 21, 2014.<sup>80</sup>

The FCC press team worked with the Chairman's senior staff to draft a media prep document on Tuesday, November 18, 2014 for a Friday press conference.<sup>81</sup> The document makes clear that FCC staff believed additional comment to be necessary.<sup>82</sup> Specifically, the draft prep document references the need for additional public comment several times:

**Q:** Does the President's letter affect the timing of the rules? Previously you said you'd have rules by the end of the year.

**A:** [W]e have recently come to the conclusion that more work will be needed on these complex issues, including possibly additional public comment.

**Q:** What sorts of questions have arisen that will require additional public comment?

**A:** There are a number of substantive issues that would benefit from more public comment. Questions regarding forbearance and the application of Open Internet rules to mobile, for example.

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**Q:** Do you plan on a Further Notice to strengthen the record?

**A:** It's definitely one of the options we are currently considering to develop a strong legal record.

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<sup>78</sup> E-mail from Claude Aiken, Fed. Commc'ns Comm'n to Joel Taubenblatt et al., Fed. Commc'ns Comm'n (Nov. 17, 2014) (HSGAC-OI-013519-20).

<sup>79</sup> See WCB Weekly Planning (summarizing items under consideration and the deadlines for drafting and consideration by Chairman Wheeler) (HSGAC-OI-028231).

<sup>80</sup> E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Zachary Ross, Fed. Commc'ns Comm'n (November 14, 2014) (HSGAC-OI-032489).

<sup>81</sup> E-mail from Kim Hart, Fed. Commc'ns Comm'n, to Daniel Alvarez et al., Fed. Commc'ns Comm'n (Nov. 18, 2014) (HSGAC-OI-13562-73).

<sup>82</sup> *Id.*



**Q:** The WSJ reported that the record was thin and you would seek additional comment? Is that true and how *do you need to beef up the record?* (emphasis added).

**A:** Yes. The Commission has been examining a number of legal options, including a hybrid approach and Title II reclassification. Over the past few weeks, a number of substantive questions have been raised and it has become clear that Commission staff need more time to study the legal, technical and policy implications of different legal theories and that the Commission record needs to be beefed up in multiple areas, including whether the FCC has the current authority to cover mobile under Title II. (emphasis added).

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**Q:** How does Title II affect the FCC's ability to apply Open Internet rules to mobile? Do you plan to expand new neutrality rules to mobile carriers?

**A:** The use of Title II authority . . . raises questions that are less than fully developed in the record, specifically whether current laws and regulations give the FCC jurisdiction over mobile IP under Title II.<sup>83</sup>

Yet, by November 19, it appears that the FCC's plan to seek further comment had changed. Career professional staff expressed confusion upon receiving feedback on the draft PN, writing "my sense is that the scope of this PN is going to be narrowed substantially, potentially to include solely the 332 CMRS [commercial mobile radio service] definition issue."<sup>84</sup> Two days later, on November 21, General Counsel Jonathan Sallet and Chairman Wheeler's Chief of Staff, Ruth Milkman, discussed with the FCC media team how best to defend the decision not to issue a PN.<sup>85</sup> A media aide pointed out to her colleagues that the FCC needed a better answer for why additional public comments were unnecessary, writing: "NEED MORE ON WHY WE NO LONGER THINK RECORD IS THIN IN SOME PLACES."<sup>86</sup> Mr. Sallet responded, referring to small group meetings conducted by FCC staff: "I think you want to point to recent ex partes and potentially we should consider whether some group meetings would be helpful."<sup>87</sup>

<sup>83</sup> *Id.*

<sup>84</sup> E-mail from Joel Taubenblatt, Fed. Commc'ns Comm'n, to Jennifer Salhus, Fed. Commc'ns Comm'n & Daniel Ball, Fed. Commc'ns Comm'n (Nov. 19, 2014) (HSGAC-OI-013599). The definition of CMRS relates to the classification decision for mobile broadband Internet.

<sup>85</sup> E-mail from Kim Hart, Fed. Commc'ns Comm'n, to Jonathan Sallet, Fed. Commc'ns Comm'n (Nov. 21, 2014) (HSGAC-OI-18251-53).

<sup>86</sup> *Id.*

<sup>87</sup> E-mail from Jonathan Sallet, Fed. Commc'ns Comm'n, to Kim Hart, Fed. Commc'ns Comm'n (Nov. 23, 2014) (HSGAC-OI-18251-53).



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**Item 5: Q&A document prepared by FCC media team and general counsel for press inquiries (Dec. 1, 2014)**

Q: You indicated that parts of the record were thin and needed to be beefed up. The Chairman also said at the last press conference that he wants to make sure he has a fulsome record to support whatever rules he puts forward. Are you now saying you don't need more comment in the record?

A: We of course welcome all comments and feedback from all parties on this important issue. [NEED MORE ON WHY WE NO LONGER THINK RECORD IS THIN IN SOME PLACES -- I think you want to point to recent ex partes and potentially we should consider whether some group meetings would be helpful]

Q: I hear staff has been calling some outside parties asking them to submit more comment on specific question. That seems like you're hand-selecting the comments you need to bolster the case for the rules you plan to propose. Why didn't you pose those questions for everyone to provide feedback?

A: The ex parte process is helpful, of course; the staff is also taking meetings that are requested by outside parties to discuss substantive issues.

In an effort to “beef up the record,” General Counsel Jonathan Sallet solicited meetings with certain outside groups such as the Center for Democracy and Technology.<sup>88</sup> He also solicited a meeting in November 2014 with Marvin Ammori, an outspoken net neutrality activist.<sup>89</sup> Reflecting the importance of the meeting—it had been solicited by General Counsel Sallet—another meeting attendee asked for “a list of questions you’d like to cover in our conversation, or some other sort of agenda.”<sup>90</sup> In the normal course of business, the request would typically be the reverse—the meeting request would originate from an outside party and the FCC employee would ask for an agenda. Yet, the FCC solicited these meetings to “beef up the record” to support a rulemaking process for Title II regulations.

Looking for evidence to justify the scrapped PN to the press, on December 1, the FCC’s media team asked senior FCC staff if “additional comments filed since early November address some of the outstanding questions, i.e., mobile and forbearance?”<sup>91</sup> Staff was only able to identify seven “OI mobile filings from the past two months.”<sup>92</sup> In other words, the FCC staff

<sup>88</sup> E-mail from Jonathan Sallet, Fed. Commc’ns Comm’n, to Nuala O’Connor, President & CEO, Center for Democracy & Technology (Nov. 26, 2014) (writing “[i]t would be great if CDT staff could come in to meet with Stephanie on OI issues, as we discussed”) (HSGAC-OI-014730).

<sup>89</sup> E-mail from Jonathan Sallet, Fed. Commc’ns Comm’n, to Marvin Ammori, Ammori Group (Nov. 11, 2014) (“Marvin: Would you be able to come in to see us next week to talk about how the Commission might move forward on its Open Internet proceeding? Thanks, Jon”) (HSGAC-OI-008120).

<sup>90</sup> E-mail from Alan Davidson, Vice President, New America, to Jennifer Tatel, Associate General Counsel, Fed. Commc’ns Comm’n (Nov. 14, 2014) (HSGAC-OI-010130-31).

<sup>91</sup> E-mail from Kim Hart, Fed. Commc’ns Comm’n, to Jonathan Sallet, Fed. Commc’ns Comm’n & Ruth Milkman, Fed. Commc’ns Comm’n (Dec. 1, 2014) (HSGAC-OI-18251-52).

<sup>92</sup> *Id.*; E-mail from Jennifer Salhus, Fed. Commc’ns Comm’n, to Michael Janson, Fed. Commc’ns Comm’n & Daniel Ball, Fed. Commc’ns Comm’n (HSGAC-OI-18366); E-mail from Michael Janson, Fed. Commc’ns Comm’n, to Daniel Ball, Fed. Commc’ns Comm’n (HSGAC-OI-18366-67).



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could not establish an adequate basis to argue that recent public comments—that is, comments filed around the time of the President’s statement—provided a sufficient justification for shifting approaches.<sup>93</sup>

The FCC’s Public Notice was never submitted to the Federal Register. The FCC never issued an FNPRM. Instead, after identifying nine separate areas in which additional comments were required, Chairman Wheeler chose to leave the record inadequate, abandon the PN that was carefully drafted by career professional staff, and forge ahead with the reclassification of broadband as a telecommunications service. He did so with the FCC staff aware of “serious” APA concerns, sacrificing regulatory certainty for political expediency.

#### IV. THE FCC EXHIBITED A LACK OF TRANSPARENCY RELATING TO ITS OPEN INTERNET ORDER

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Federal law contains a number of provisions designed to ensure transparency in government. Congressional oversight of executive branch activities is another mechanism for ensuring the integrity of government processes. In promulgating its OI Order, the FCC burdened congressional oversight efforts and appeared to err on the side of secrecy with *ex parte* filings instead of transparency.

##### A. The FCC withheld drafts of the Open Internet Order requested by Chairman Johnson

In February 2014, Chairman Johnson requested that the FCC produce the draft OI Order that was under consideration by the FCC in the fall of 2014—at the time of the President’s statement.<sup>94</sup> On April 8, 2015, FCC Chairman Wheeler responded by suggesting that no such draft existed. He wrote: “[T]here was not a draft net neutrality proposal that was finalized for circulation to my fellow Commissioners in late November or early December.”<sup>95</sup>

Although this carefully scripted answer may indeed be true—in that there was no proposal circulated to the commissioners in that period—it conveniently ignores the fact that the FCC possesses drafts of the OI Order from that timeframe.<sup>96</sup> (See Appendix A) As discussed above, it was not due to a lack of hard work by the career professional staff at the FCC that these drafts did not make it to the commissioners. Instead, a draft was never circulated among the

<sup>93</sup> See *supra* note 16.

<sup>94</sup> Appendix C, Ex. 1, Letter from Ron Johnson, S. Comm. on Homeland Sec. & Gov’t Affairs, to Tom Wheeler, Fed. Commc’ns Comm’n (Feb. 9, 2015).

<sup>95</sup> Appendix C, Ex. 3, Letter from Tom Wheeler, Fed. Commc’ns Comm’n, to Ron Johnson, S. Comm. on Homeland Sec. & Gov’t Affairs (Apr. 8, 2015).

<sup>96</sup> E-mail from Claude Aiken, Fed. Commc’ns Comm’n, to Jonathan Sallet et al., Fed. Commc’ns Comm’n (Nov. 5, 2014, 10:35PM) (HSGAC-OI-006693) (emphasis added).





commissioners because the Chairman opted to change course and abandoned his original plan after the White House's intervention.

Several documents produced to the Committee reference the existence of drafts of the Open Internet proposal prior to the President's statement in support of Title II. For example, in one email to General Counsel Jonathan Sallet and other senior FCC leaders dated November 5, 2014, an FCC employee wrote: "[H]ere is an updated version of the OI draft that includes all of the outstanding component parts. While still a work in progress, this is the most comprehensive and complete draft to date."<sup>97</sup> Mr. Sallet forwarded this e-mail to another FCC employee, asking him to print a hard copy.<sup>98</sup> Although this e-mail included an attachment with the draft proposal, the attachment was withheld from the Committee when the FCC produced documents.

Other documents similarly show that the FCC considered additional drafts of its Open Internet proposal.<sup>99</sup> FCC staff even prepared summary documents to compare the changes made in various drafts of the proposal.<sup>100</sup> Neither the drafts nor the summary documents were produced to the Committee despite being responsive to Chairman Johnson's initial request. The majority staff repeatedly tried to obtain these documents from the FCC.<sup>101</sup> However, the FCC indicated that it would prefer to offer a briefing on the subject, rather than provide responsive documents.<sup>102</sup> In addition to the drafts of the proposal, the FCC also circulated drafts of a potential PN in November 2014 requesting further comment

**"I'm proud of the process that the commission ran to develop the Open Internet Order. It was one of the most open and most transparent in commission history."  
– Chairman Wheeler, Testimony before the House Oversight and Gov't Reform Comm., March 17, 2015**

<sup>97</sup> *Id.*

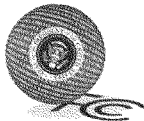
<sup>98</sup> E-mail from Jonathan Sallet, Fed. Commc'ns Comm'n, to Richard Williams, Fed. Commc'ns Comm'n (Nov. 6, 2014) (HSGAC-OI-006693).

<sup>99</sup> See, e.g., E-mail from Daniel Ball, Fed. Commc'ns Comm'n, to Joel Taubenblatt, Fed. Commc'ns Comm'n (Nov. 7, 2014) (HSGAC-OI-002721); E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Jonathan Sallet et al., Fed. Commc'ns Comm'n (Oct. 31, 2014) (HSGAC-OI-005003–04).

<sup>100</sup> E-mail from Thomas Parisi, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 5, 2014) (HSGAC-OI-029491).

<sup>101</sup> E-mail from staff of the S. Homeland Sec. & Gov't Affairs Comm., to staff of the Fed. Commc'ns Comm'n (April 17, 2015); E-mail from staff of the S. Homeland Sec. & Gov't Affairs Comm., to staff of the Fed. Commc'ns Comm'n (May 21, 2015); E-mail from staff of the S. Homeland Sec. & Gov't Affairs Comm., to staff of the Fed. Commc'ns Comm'n (June 2, 2015).

<sup>102</sup> E-mail from staff of the Fed. Commc'ns Comm'n, to the staff of the S. Homeland Sec. & Gov't Affairs Comm. (June 5, 2015).



on select policy issues.<sup>103</sup> Portions of the draft PN were provided to the Committee; however, the FCC failed to produce a full draft of the PN.<sup>104</sup>

#### ***B. The FCC circumvented ex parte communication requirements***

The FCC must obey the requirements of notice-and-comment rulemaking, which includes ensuring that the public has access to a record of all *ex parte* communications related to an agency proceeding.<sup>105</sup> The intention of these requirements is to bring transparency and accountability into the regulatory process. Throughout the FCC's process of drafting its OI Order, the Commission circumvented transparency by avoiding compliance with *ex parte* communication requirements.

By definition, an *ex parte* communication is "an oral or written communication not on the public record with respect to which reasonable prior notice to all parties is not given."<sup>106</sup> A general exclusion exists for "status report" requests.<sup>107</sup> "At the FCC, '*ex parte*' describes a communication directed to the merits or outcome of a proceeding" but which was not said or written to the public.<sup>108</sup> Any communication from a Member of Congress or the executive branch of the federal government is considered *ex parte* if it is "of substantial significance and clearly intended to affect the ultimate decision."<sup>109</sup> Although a 1991 opinion from the Justice Department's Office of Legal Counsel opines that White House officials may advocate for a particular policy position in FCC rulemakings, the opinion also cautions that "White House staff members should avoid even the mere appearance of interest or influence—and the easiest way to do so is to avoid discussing matters pending before the independent regulatory agencies."<sup>110</sup>

<sup>103</sup> See E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Kristine Fargotstein, Fed. Commc'ns Comm'n (Nov. 17, 2014) (seeking additional comments because "[t]he response to the NPRM has brought to light additional issues that warrant further comment.") (HSGAC-OI-032431-32).

<sup>104</sup> See e.g., E-mail from Melissa Krikell, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 17, 2014) (describing the need for additional comment on forbearance "on the extent to which forbearance should apply if the Commission were to classify mobile broadband Internet access service as a CMRS service subject to Title II.") (HSGAC-OI-032465-66); E-mail from Kristine Fargotstein, Fed. Commc'ns Comm'n, to Claude Aiken, Fed. Commc'ns Comm'n (Nov. 17, 2014) (outlining additional questions related to Interconnection for the PN) (HSGAC-OI-032431); *But see*, E-mail from Claude Aiken, Fed. Commc'ns Comm'n, to Julie Veach et al., Fed. Commc'ns Comm'n (Nov. 17, 2014, 10:25PM) (describing an attached draft Public Notice "that is due to go to OCH on 11/19", which was not provided to the Committee) (HSGAC-OI-032423).

<sup>105</sup> 47 CFR 1.1206(b)(2) (2016).

<sup>106</sup> 5 U.S.C. 551; *see also*, 47 C.F.R. 1.1202.

<sup>107</sup> 5 U.S.C. 551; *see also*, 47 C.F.R. 1.1202(a).

<sup>108</sup> Fed. Commc'ns Comm'n., Ex Parte Resources, <https://www.fcc.gov/proceedings-actions/ex-parte/general/ex-parte-resources> (last visited Feb. 5, 2016); 47 CFR 1.1202 (2016).

<sup>109</sup> 47 C.F.R. 1.1206(b)(3).

<sup>110</sup> O.L.C. Opinion, *supra* note 16 at 4 (emphasis added).



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At the FCC, a summary of the written or oral *ex parte* communication must be filed in the record so that the public and stakeholders have the opportunity to review and comment.<sup>111</sup> For instance, after President Obama's statement supporting Title II regulation of the Internet and after senior White House official Jeffrey Zients met with Chairman Wheeler, the FCC entered *ex parte* filings into the record for both communications.<sup>112</sup> During the course of the OI Order drafting process, however, documents produced to the Committee revealed other examples in which FCC senior staff either did not file an *ex parte* notice or reasoned that one was not necessary.<sup>113</sup>

In one instance, a reporter questioned why *ex parte* notices had not been filed for Chairman Wheeler's dozen or more meetings at the White House.<sup>114</sup> In response to this inquiry, the FCC media team conferred with senior staff in Chairman Wheeler's office. In an effort to justify the decision not to file *ex parte* notices, Philip Verveer, Senior Counsel to the Chairman asserted, "I assume the answer is that there literally was no advocacy" during the meetings between Chairman Wheeler and White House personnel.<sup>115</sup> The reporter responded that he found that "hard to believe."<sup>116</sup>

The documents reviewed by the Committee make clear that Chairman Wheeler regularly communicated with presidential advisors. None of the communications reviewed by the Committee were submitted to the FCC's formal record in the form of *ex parte* notices although the OI Order was clearly discussed.<sup>117</sup> One email between Chairman Wheeler and Jeffrey Zients

<sup>111</sup> 47 C.F.R. 1.1206(b)(1)-(2); see e.g., Protecting and Promoting the Open Internet, 79 Fed. Reg. 37448, 37472 (proposed May 15, 2014) (to be codified at 47 C.F.R. 8) (requiring that *ex parte* filings be submitted to the record within two days of the communication).

<sup>112</sup> *Ex Parte* for President Barack Obama and Jeffrey Zients, Protecting and Promoting the Open Internet (GN Docket No. 14-28) (Nov. 10, 2014).

<sup>113</sup> E-mail from Stephanie Weiner, Fed. Commc'ns Comm'n, to Markham Erickson, Partner, Steptoe & Johnson LLP (Nov. 19, 2014) (discussing OI process but no *ex parte* was filed) (HSGAC-OI-013618); E-mail from Matthew DelNero, Fed. Commc'ns Comm'n, to Praveen Goyal, Counsel, Hogan Lovells US LLP (Nov. 12, 2015) (rationalizing that no *ex parte* was necessary) (HSGAC-OI-009711).

<sup>114</sup> E-mail from Brooks Boliek, Reporter, Politico, to Kim Hart, Press Secretary, Fed. Commc'ns Comm'n (Nov. 19, 2014) (HSGAC-OI-013791).

<sup>115</sup> E-mail from Philip Verveer, Fed. Commc'ns Comm'n, to Kim Hart, et al., Fed. Commc'ns Comm'n (Nov. 19, 2014) (HSGAC-OI-013791).

<sup>116</sup> E-mail from Kim Hart, Fed. Commc'ns Comm'n, to Philip Verveer, et al., Fed. Commc'ns Comm'n (Nov. 19, 2014) (HSGAC-OI-013791).

<sup>117</sup> E-mail from Tom Wheeler, Fed. Commc'ns Comm'n, to David Edelman, Fed. Commc'ns Comm'n (April 23, 2014) (HSGAC-OI-001232); E-mail from Tom Wheeler, Fed. Commc'ns Comm'n, to Jeffrey Zients, Exec. Office of the President, John Podesta, Exec. Office of the President, Jason Furman, Exec. Office of the President, Tom Power, Exec. Office of the President, & David Edelman, Exec. Office of the President (April 24, 2014) (HSGAC-OI-001223); E-mail from Tom Wheeler, Fed. Commc'ns Comm'n, to Jeffrey Zients, Exec. Office of the President & Jason Furman, Exec. Office of the President (April 29, 2014) (HSGAC-OI-001227); E-mail from Tom Wheeler, Fed. Commc'ns Comm'n, to Jeffery Zients, Exec. Office of the President, Jason Furman, Exec. Office of the



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and Jason Furman makes reference to a prior conversation about the OI Order.<sup>118</sup> *Ex parte* notices were not filed for either the email or the conversation.

**Item 6: Email from Chairman Wheeler to Jeffrey Zients & Jason Furman (Apr. 29, 2014)**

**From:** TW  
**To:** [REDACTED]@who.eop.gov; [REDACTED]@cea.eop.gov  
**Subject:** Fw: FINAL NCTA  
**Date:** Tuesday, April 29, 2014 4:38:00 PM  
**Attachments:** OI blog 4 29 FINAL FOR POSTING.docx

As per our discussion: this is this afternoon's blog post on the Open Internet NPRM.

All options on the table...we are seeking comments and input...following the court's blueprint.

T

**Item 7: Email from Chairman Wheeler to Jeffrey Zients, Jason Furman, & Tom Power (Apr. 23, 2014)**

**From:** TW  
**Sent:** Wednesday, April 23, 2014 10:15 PM  
**To:** [REDACTED]@who.eop.gov; [REDACTED]@who.eop.gov>; [REDACTED]@cea.eop.gov; [REDACTED]@cea.eop.gov>; [REDACTED]@postp.eop.gov; [REDACTED]@postp.eop.gov>  
**Subject:** NYT story is wrong

The NYT is moving a story that the FCC is gutting the Open Internet rule. It is flat out wrong. Unfortunately, it has been picked up by various outlets without checking.

Tomorrow we will circulate to the Commission a new Open Internet proposal that will restore (and in in the case of transparency which was allowed to stand by the court, expand) the concepts in the original Net Neutrality Order in a manner consistent with the court's ruling in January.

There is no "turnaround in policy." We are implementing the same policies in a manner that will pass court scrutiny. We have told the NYT they have it wrong.

The same rules will apply to all Internet content. As with the original Open Internet rules, and consistent with the court's decision, behavior that harms consumers or competition will not be permitted.

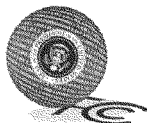
We are moving a statement containing these points to the media right now.

Please call me if you have any questions. [REDACTED] is my mobile.

T

President, Tom Power, Exec. Office of the President, & John Podesta, Exec. Office of the President (April 29, 2014) (HSGAC-OI-001233).

<sup>118</sup> E-mail from Tom Wheeler, Fed. Comm'n's Comm'n, to Jeffrey Zients, Exec. Office of the President & Jason Furman, Exec. Office of the President (April 29, 2014) (HSGAC-OI-001227).



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## Item 8: Email from Chairman Wheeler to White House Advisors (Apr. 24, 2014)

**From:** TW  
**Sent:** Thursday, April 24, 2014 06:17 PM  
**To:** [REDACTED]@who.eop.gov; [REDACTED]@who.eop.gov; [REDACTED]@who.eop.gov; [REDACTED]@who.eop.gov; [REDACTED]@cea.eop.gov; [REDACTED]@cea.eop.gov; [REDACTED]@postp.eop.gov; [REDACTED]@postp.eop.gov; [REDACTED]@who.eop.gov; [REDACTED]@who.eop.gov  
**Subject:** Fw: CNET: Calm down: FCC's position on Net neutrality hasn't changed

Gentlemen -

This is the most thoughtful explanation of what has been going on with the Open Internet. I thought you'd want to see it. She is exactly right.

We have been spending the day with congressional calls, and editorial board and reporter calls.

I just wanted you to have this so you'd see a realistic analysis of what's really going on.

T

**From:** Meribeth McCarrick  
**Sent:** Thursday, April 24, 2014 05:52 PM  
**To:** Gigi Sohn; TW; Shannon Gilson; Neil Grace; Mark Wigfield; Sara Morris; Jonathan Sallet; Maria Kirby; Renee Gregory; Daniel Alvarez; Ruth Milkman; Stephanie Weiner; Rochelle Cohen; Julie Veach  
**Subject:** CNET: Calm down: FCC's position on Net neutrality hasn't changed

**Calm down: FCC's position on Net neutrality hasn't changed**  
**There's been a lot of confusion about what the FCC is or is not proposing for its rewrite of its Open Internet rules. CNET's Marguerite Reardon breaks it down.**  
**by Marguerite Reardon**  
**April 24, 2014 2:10 PM PDT**  
<http://www.cnet.com/news/fccs-position-on-net-neutrality-hasnt-changed/>  
 When it comes to discussing the FCC's recent proposal for rewriting its Net neutrality rules, everyone needs to take a deep breath, slow down and check their facts, according to FCC chairman Tom Wheeler, whose agency seems to have a knack for inadvertently exciting the public over its proposed policy plans.



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## Item 9: Email from Chairman Wheeler to Jeffrey Zients, Jason Furman, Tom Power, &amp; John Podesta (Apr. 29, 2014)

**From:** TW  
**Sent:** Tuesday, April 29, 2014 7:52 PM  
**To:** 'Jeff Zients'; 'Jason Furman'; 'Tom Power'; 'John D. Podesta'  
**Subject:** Open Internet update  
**Attachments:** NCTA Final4-29.docx

Gentlemen -

Below is the link to today's blog further explaining the Open Internet NPRM. The press reaction has been what we'd hoped, that I have clarified previous misconceptions about how the proposal would somehow gut the Open Internet

Attached is my speech to NCTA tomorrow. The first two pages are about Open Internet - a message delivered to the broadband providers as to what will be expected.

Message in both: (1) it is a proposal on which we seek comment, (2) all options are on the table, including Title II, and (3) I have flat out expressed skepticism that we'd find "commercial reasonableness" to be a route to exceptions to the rule for special deals and prioritization.

As I have said since February, the proposal is designed to deliver on the goals of the 2010 Open Internet Order (which, you'll recall, included a reasonableness test) and to do so in a manner that follows the D.C. Circuit's roadmap (and hopefully thus avoids litigation).

The President has supported the Open Internet and anti-discrimination. Just like he supported the 2010 order with its reasonableness test there is no need to no change with this proposal. I believe he can say that we are using current law to its fullest (and in a manner that was prescribed by the court) to assure an Open Internet and anti-discrimination. The next step is to change the law, even Title II has a "just and reasonable" test.

I hope this is helpful.

The initial coverage has been helpful and the feedback from the public interest groups better. I'll send you some clips in a moment.

T

While neither the OLC Opinion nor the FCC rules further define the threshold for requiring an *ex parte* filing—beyond the communication being of “substantial significance and clearly intended to affect the ultimate decision”—emails between Chairman Wheeler and White House senior staff show the FCC’s efforts to justify and further explain actions taken in relation to the OI Order.<sup>119</sup> Clearly, given the importance of this issue, the FCC and the White House should have taken great pains to even avoid the appearance that the White House influenced the FCC’s independent rulemaking. As it is, the lack of transparency surrounding these communications is troubling and raises further questions about the development of the FCC’s order.

<sup>119</sup> See e.g., E-mail from Tom Wheeler, Fed. Commc’ns Comm’n, to David Edelman, Fed. Commc’ns Comm’n (April 23, 2014) (clarifying that there is “no ‘turnaround in policy’”) (HSGAC-OI-001232); E-mail from Tom Wheeler, Fed. Commc’ns Comm’n, to Jeffrey Zients, Exec. Office of the President, Jason Furman, Exec. Office of the President, Tom Power, Exec. Office of the President, & John Podesta, Exec. Office of the President (April 29, 2014) (justifying that the FCC’s proposed OI rule can still be supported by the President) (HSGAC-OI-001233).



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## V. CONCLUSION

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In February 2015, the *Wall Street Journal* reported that the President’s “vision for regulating high-speed Internet traffic” “swept aside more than a decade of light-touch regulation of the Internet and months of work by [FCC Chairman] Wheeler toward a compromise.”<sup>120</sup> Chairman Wheeler shortly thereafter “lined up behind Mr. Obama” and announced that the FCC would follow the President’s orders—it would classify the Internet under Title II of the Communications Act.<sup>121</sup> The documents that inform the Committee’s inquiry confirm this report.

An analysis of documents produced to the Committee in response to Chairman Johnson’s request shows that the FCC bent to the political pressure of the White House, abandoning its work on a hybrid approach to “pause” and then pivot to reclassify broadband as a telecommunications service, subjecting broadband providers to regulation under Title II of the Communications Act. The FCC’s staff worried that the process to adopt President Obama’s preferred policy approach violated the Administrative Procedure Act. Most fundamentally, throughout this process—as the FCC shifted to a Title II approach and then responded to congressional oversight—it failed to live up to standards of transparency.

It should be highly concerning that an independent agency like the FCC could be so unduly influenced by the White House, particularly on an issue that touches the lives of so many Americans and has such a significant impact on a critical sector of the United States economy. Documents produced to the Committee clearly show that the career professional staff at the FCC worked diligently on the Commission’s OI Order, despite its significant and last-minute change in direction. It is also clear that career professional staff worked expeditiously and thoroughly on the Commission’s planned Public Notice, despite its ultimate abandonment by FCC leadership. Had the White House not inserted itself into the formal FCC rulemaking process, it is probable that the Open Meeting in December would have included the OI Order. At the very least, if the FCC had issued a Public Notice, the record would presumably have been much more informed. Politics should never trump policy, especially not when an agency, like the FCC, was created for the expressed purpose of being independent and above the political fray.

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<sup>120</sup> Nagesh *supra* note 1.

<sup>121</sup> See Nagesh *supra* note 1.



**MEMORANDUM**

February 24, 2016

**To: Members of the Committee on Homeland Security and Governmental Affairs**  
**From: Committee on Homeland Security and Governmental Affairs Minority Staff**  
**Re: Minority Staff Findings Concerning the Department of Labor's Proposed Conflict of Interest Rule**

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**I. Executive Summary**

On February 5, 2015, the Chairman of the U.S. Senate Committee on Homeland Security and Governmental Affairs Committee initiated an investigation into the Department of Labor's efforts to change the fiduciary rules related to certain retirement plans. On April 20, 2015, the Labor Department issued a proposed Conflict of Interest rule for fiduciaries. The proposed rule would update the definition of a "fiduciary" under the Employee Retirement Income Security Act of 1974 (ERISA) to prevent conflicts of interest in advice provided for employee savings plans, including 401(k) and Individual Retirement Accounts. The issuance of a proposed rule triggered a notice and comment period that allows stakeholders to submit comments before the final rule is issued. To date, the rule making is still ongoing, and the final rule has not yet been issued. The purpose of this memorandum is to provide the findings of the Committee's minority staff regarding the Chairman's investigation.

As the Labor Department is still engaged in the process of finalizing this rule, the record before the Committee is incomplete and does not reflect the Labor Department or any other agency's final position regarding the rule. As such, broad conclusions about the policy impact or the content of the final rule are premature.

However, a review of the record demonstrates that the Labor Department went beyond the requirements of the Administrative Procedure Act and conducted an extensive process to solicit comments and technical assistance from other federal agencies with expertise that may be relevant to the rule. This process started before the Labor Department proposed a revised rule in 2015 and included at least 52 meetings or phone calls with the Securities and Exchange Commission (SEC), the Financial Industry Regulatory Authority (FINRA), the Department of the Treasury (Treasury), and the Office of Management and Budget (OMB). This process also included at least eight meetings or phone calls between the Secretary of Labor Tom Perez and SEC Chair Mary Jo White. As a result of these consultations, the Labor Department considered and incorporated comments and technical assistance before the proposed rule was published in the *Federal Register* on April 20, 2015.

In addition, the Labor Department made a significant effort to solicit input from the public and other stakeholders on the proposed rule. While conducting a formal regulatory review of the proposed rule, OMB's Office of Information and Regulatory Affairs held 21 meetings with stakeholders, including industry and consumer advocates. After extending the public comment period and hosting a four-day public hearing on the proposed rule, the Labor Department also



received a total of 3,134 comments, including 30 petitions encompassing an additional 386,889 comments.

## II. Background

The Department of Labor has the authority under ERISA to regulate fiduciary standards to protect the interests of retirement plan participants and their beneficiaries.<sup>1</sup> The Labor Department's Employee Benefits Security Administration (EBSA) is responsible for ensuring compliance with the provisions of ERISA. Under ERISA, a person who provides retirement investment advice has a fiduciary obligation and must act in the sole interest of the plan participant. The Labor Department issued regulations in 1975 to define investment advice according to a five-part test, and an advisor is held to the best interest standard if the advice meets each part of the test.<sup>2</sup>

Since the passage of ERISA 42 years ago, retirement plans provided to employees have largely changed from "defined benefit plans," such as traditional pensions, to "defined contribution plans," such as 401(k) retirement accounts. Many investment professionals and advisors for defined contribution plans give retirement investment advice that falls outside the current, narrowly-tailored definition of investment advice under ERISA and are not obligated to adhere to ERISA's best interest standard. Conflicts of interest may arise in this context if retirement investment advice is given in order to provide greater commissions to the investment advisor and is not made in the best interest of the client.

To address this issue, in October 2010, the Labor Department proposed a Conflict of Interest rule to broaden the definition of a "fiduciary" under ERISA.<sup>3</sup> The purpose of the rule was to prevent conflicts of interest by applying the best interest standard to investment advisors providing advice for defined contribution plans. Under the new definition, investment advisors such as broker-dealers would be considered fiduciaries under ERISA and would be required to abide by a best interest standard. During the notice and comment period for the proposed 2010 rule, stakeholders, Members of Congress, and the public raised concerns about the proposed rule and requested the agency to allow more opportunity for input. The Labor Department subsequently withdrew the rule in September 2011 to address those concerns with a goal of reintroducing a draft rule in early 2012.<sup>4</sup>

On April 20, 2015, the Labor Department proposed a revised Conflict of Interest rule on the definition of "fiduciary" under ERISA.<sup>5</sup> The proposed rule initially provided for a 75-day comment period from April 20, 2015 to July 6, 2015. After receiving requests for additional time to submit input on the revised rule, the Labor Department extended the comment period by two weeks in July and held a four-day hearing during the week of August 10, 2015. The Labor

<sup>1</sup> Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001–1453 (2016).

<sup>2</sup> 29 U.S.C. § 1104 (2016).

<sup>3</sup> 75 Fed. Reg. 65263, 65278 (proposed October 22, 2010).

<sup>4</sup> Department of Labor, *US Labor Department's EBSA to Re-Propose Rule on Definition of a Fiduciary* (Sept. 19, 2011)(11-1382-NAT).

<sup>5</sup> 80 Fed. Reg. 21927, 21960 (proposed April 20, 2015).

Department then re-opened the comment period again for an additional two weeks for additional public testimony and comments after the hearing.<sup>6</sup> In total, there were over 100 days for the public to comment on the draft rule.

While the rulemaking process is ongoing, the Labor Department has indicated that the final rule would become effective 60 days after publication in the *Federal Register*, and the requirements of the rule would generally become applicable eight months after publication of a final rule.

On February 5, 2015, the Chairman of the U.S. Senate Committee on Homeland Security and Governmental Affairs Committee began an inquiry into reported efforts of the Labor Department to change fiduciary rules related to retirement plans.<sup>7</sup> At this time, the Department of Labor had not yet issued a proposed rule, but the majority initiated the investigation by citing concerns of the financial industry and others regarding the policy impact a revised rule could have.<sup>8</sup> Subsequently, Chairman Johnson sent letters to the SEC, FINRA, Treasury, and OMB seeking information regarding the ongoing rulemaking process. In total, Chairman Johnson sent nine information request letters to federal agencies and in response received sixteen letter responses; two briefings with Labor Department officials; and 12,763 pages of agency documents, including documents reviewed during two *in camera* reviews. An appendix to this memorandum includes the formal correspondence between the Committee and the entities that received requests for information.

As the Labor Department is still engaged in the process of finalizing this rule, the record before the Committee is incomplete and does not reflect the Labor Department or any other agency's final position regarding the rule. As such, broad conclusions about the policy impact or the content of the final rule are premature.

### **III. The Department of Labor's Process to Solicit Comments and Technical Assistance from Other Agencies was Extensive.**

The Department of Labor and other federal agencies have different statutory responsibilities with respect to regulating investment advisors and the financial securities market. While the Labor Department and Treasury are responsible for enforcing ERISA to protect the interests of retirement plan participants and beneficiaries, SEC is responsible for regulating many aspects of the financial securities market in accordance with the Investment Advisers Act of 1940. Similarly, FINRA, a self-regulatory organization of securities brokers, requires securities brokers and dealers to give investment advice that is suitable for the customer.<sup>9</sup>

<sup>6</sup> 80 Fed. Reg. 34869, 34871 (June 18, 2015).

<sup>7</sup> Letter from Senate Committee on Homeland Security and Governmental (HSGAC) Chairman Johnson to Department of Labor Secretary Thomas Perez (Feb. 5, 2015).

<sup>8</sup> *Id.*, citing Mark Schoeff, *DOL Proposal of Fiduciary-Duty Rule Delayed Again*, Investment News, (May 28, 2014) (quoting Securities Industry and Financial Markets Association President and Chief Executive Kenneth Bentsen Jr. and Financial Services Institute Vice President Chris Paulitz, among others).

<sup>9</sup> FINRA Rule 2111 (2014).

The Administrative Procedure Act prescribes requirements for stakeholder input through notice and comment periods, and these requirements do not require interagency consultation before an agency proposes a rule. Agencies, however, regularly do consult with each other in an effort to improve the quality of a proposed rule. Further, OMB's Office of Information and Regulatory Affairs (OIRA) conducts a formal review process and ensures for significant rules agencies have the opportunity to weigh in during the proposed and final rulemaking stages.

According to information obtained by the Committee, the Labor Department went beyond the requirements of the Administrative Procedure Act and conducted an extensive process to solicit comments and technical assistance from other federal agencies with expertise that may be relevant to the rule. These consultations started after the Labor Department withdrew the 2010 draft rule, continued through the years leading up to the proposal of the revised rule on April 20, 2015, and included at least 52 meetings or phone calls with the SEC, FINRA, and Treasury. As a result of these consultations, the Labor Department considered and incorporated comments and technical assistance before the proposed rule was published in the *Federal Register*.<sup>10</sup>

In particular, the Labor Department engaged with the SEC to solicit input regarding the proposed rule on several occasions. Between November 2013 and January 2015, Labor Department officials from EBSA and SEC officials from many offices conducted at least 21 meetings or phone calls regarding multiple aspects of the conflict of interest rulemaking.<sup>11</sup> They discussed the proposed rule, securities regulations, market dynamics, the exemption for principal transactions, point of sales disclosure, low-fee safe harbor, economic analysis including cost-benefit analysis, and supporting data.<sup>12</sup> Meetings during this period included the participation of 31 SEC employees from five separate SEC divisions, including the Office of the Chair, Trading and Markets, Investment Management, Economic and Risk Analysis, and the Office of the General Counsel.<sup>13</sup>

The Labor Department also engaged with FINRA to solicit input regarding the proposed rule on several occasions. Between April 13, 2011 and November 18, 2013, the Labor Department and FINRA officials conducted 31 meetings or phone calls.<sup>14</sup> Meetings during this period included the participation of 54 employees, including 26 employees from the Labor Department and 27 employees from FINRA.<sup>15</sup> Between April 4, 2014 and September 14, 2015, Labor and FINRA officials conducted an additional 18 meetings.<sup>16</sup> During this period, these meetings

<sup>10</sup> See EBSA Responses to SEC Comments (January 8, 2015)[SEC-DOL003236-SEC-DOL003239].

<sup>11</sup> Letter from the Securities and Exchange Commission Chairwoman Mary Jo White to HSGAC Chairman Johnson (May 5, 2015).

<sup>12</sup> Letter from Acting Assistant Secretary Jayaratne to HSGAC Chairman Johnson (June 15, 2015); see also Letter from the Securities and Exchange Commission Chairwoman Mary Jo White to HSGAC Chairman Johnson (July 27, 2015).

<sup>13</sup> Letter from the Securities and Exchange Commission Chairwoman Mary Jo White to HSGAC Chairman Johnson (May 5, 2015).

<sup>14</sup> Letter from FINRA Executive Vice President and Chief Legal Officer Richard Colby to HSGAC Chairman Johnson (Oct. 29, 2015).

<sup>15</sup> *Id.*

<sup>16</sup> Letter from FINRA Executive Vice President and Chief Legal Officer Richard Colby to HSGAC Chairman Johnson (Oct. 15, 2015).

included the participation of 31 employees, including 16 employees from the Labor Department and 15 employees from FINRA.<sup>17</sup> Some of the topics discussed during these meetings included potential unintended consequences of the rule, an impartial conduct standard, salary structures, litigation, and remedies.

The Labor Department also engaged with Treasury to solicit input regarding the proposed rule. Documents obtained by the Committee reflected several instances when Treasury and Labor Department officials exchanged comments about drafts of the rule and discussed the technical assistance provided by Treasury.<sup>18</sup> In a December 14, 2015 letter to the Committee, Treasury stated it “believes that DOL appropriately considered Treasury comments on the drafts during the OIRA process, including the comments specified in [Chairman Johnson’s November 12, 2015] letter.”<sup>19</sup>

Documents regarding the interaction between the Labor Department and other agencies on the proposed rule reflect occasionally frank and candid exchanges of views that would be expected during the deliberative interagency process when a proposed rule is under discussion. Since the rulemaking process is ongoing, however, the documents obtained by the Committee do not reflect the Labor Department’s final position regarding the rule.

#### **IV. OMB’s Office of Information and Regulatory Affairs Reviewed the Department of Labor’s Draft Rule, Including the Cost-Benefit Analysis and the Rule’s Consistency with Existing Federal Statutes.**

Before publication in the *Federal Register*, the Labor Department submitted the proposed rule to OIRA. OIRA ensures regulatory action is consistent with applicable laws, verifies agency policies do not conflict, and enables other relevant Federal agencies to provide their views. Much of OIRA’s regulatory oversight is governed by Executive Order (E.O.) 12866, “Regulatory Planning and Review,” and E.O. 13563, “Improving Regulation and Regulatory Review.”

When submitting a draft rule to OIRA, an agency generally provides a detailed cost-benefit analysis including an assessment of feasible alternatives to the proposed rule. During its review of the draft rule, OIRA also consults with various stakeholders. In accordance with E.O. 12866, OIRA meets with any party interested in discussing issues during the proposed and final stages of a regulatory review. Reviews are typically completed within 90 days. After conducting a review, OIRA sends the rule back to the agency. The most common type of action OIRA takes is “consistent with change,” which indicates OIRA approves of the intent of the rule but made some substantive changes. If an agency receives approval from OIRA, it may then publish the rule in the *Federal Register*. Before finalizing the rule, the agency must identify changes made to the rule between the draft submitted to OIRA for review and the final rule.

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<sup>17</sup> *Id.*

<sup>18</sup> See Proposed Best Interest Contract Exemption (Apr. 8, 2015) [SEC-DOL 005002].

<sup>19</sup> Letter from Assistant Secretary for Legislative Affairs of Treasury Anne Wall to HSGAC Chairman Johnson (Dec. 14, 2015).

OIRA received the proposed Conflict of Interest rule from the Labor Department on February 23, 2015. Between March 4, 2015 and April 10, 2015, OIRA conducted 21 stakeholder meetings.<sup>20</sup> Some of the stakeholders included Fidelity Investments, the Financial Services Roundtable, and the U.S. Chamber of Commerce.<sup>21</sup> OIRA concluded its review of the proposed rule on April 14, 2015 and sent it back to the Labor Department as “consistent with change.” In correspondence with the Committee, OIRA stated that its office “devoted the time and resources necessary to ensure the review was in accordance with the requirements of EOs 12866 and 13563. The amount of time needed to complete review on any given rule varies, but OIRA endeavors to complete the process as efficiently as possible while ensuring proper review.”<sup>22</sup>

**V. The Department of Labor Made a Significant Effort to Solicit Comments from the Public and Other Stakeholders.**

The Department of Labor engaged in an extended public notice and comment period on the proposed conflict of interest rule. Notice and comment periods provide the public and stakeholders the opportunity to offer their views and recommendations.<sup>23</sup> These comments become part of the rulemaking record on which the Labor Department must base its reasoning and conclusions.

Once the Labor Department re-proposed the revised rule, the initial comment period spanned 75 days from April 20, 2015 to July 6, 2015. After receiving requests to extend the comment period to allow for additional input to the rulemaking record, the Labor Department extended this comment period through July 21, 2015 and announced it would hold hearings during the week of August 10, 2015. The comment period was also re-opened on the day that hearing transcripts were published from September 8 to September 24, 2015.<sup>24</sup> In total, the public comment period on the draft rule was open for over 100 days.

During this process, the Labor Department received a substantial number of comments. Between April 2015 and September 2015, the Labor Department received 3,134 individual comments as well as 30 petitions encompassing an additional 386,889 comments.<sup>25</sup> 542 of these

<sup>20</sup> E.O. 12866 Meeting Records (2016).

<sup>21</sup> Other stakeholders included Personal Capital, Better Markets, American Retirement Association, Davis & Harman LLP, Consumer Federation of America, Public Investors Arbitration Bar Association, Fiduciary Institute, Securities Industry and Financial Markets Association, American Council of Life Insurers, Financial Services Institute, Franklin Square Capital Partners, Americans for Financial Reform, Insured Retirement Institute, Primerica, Investment Company Institute, and Rebalance IRA.

<sup>22</sup> Letter from OIRA Administrator Howard Shelanski to HSGAC Chairman Johnson (Jan. 20, 2016).

<sup>23</sup> Administrative Procedure Act of 1946, 5 U.S.C. §§ 551–59 (2016).

<sup>24</sup> Department of Labor, Public Hearing Announcement of Transcript Availability and Comment Period Closing Date for the Conflict of Interest Proposed Rule (Sept. 8, 2015).

<sup>25</sup> Petitioners were AARP, Financial Professionals through Softedge, New York Life Insurance, Public Citizen, Life Insurance Professionals, Close the Investment Advice Loophole, Protect our Retirement Nest Eggs, I Support the DOL Retirement Advice Rule, As Someone Saving for my Future, Independent Financial Advisors, National Association of Insurance and Financial Advisors State Associations, MoveOn.org Civic Action Individuals, Primerica Licensed Financial Professionals, U.S. Public Interest Research Group Individuals, Strengthen Retirement Advice Laws, Stop Wall Street from Draining Americans' Retirement Savings, Licensed Financial Professionals, National Association of Insurance and Financial Advisors Members, Americans for Financial Reform, CREDO

comments were received after the Labor Department re-opened the comment period. The comments represented a wide range of views from the financial services industry, consumer advocacy groups, and Members of Congress from both the House and Senate.

The Labor Department also held four public hearings on the proposed rule from August 10-13, 2015 at the Labor Department's Washington, D.C. headquarters. These hearings consisted of 25 panels featuring 41 submissions of written testimony.<sup>26</sup> The hearing transcripts, which span 1,305 pages, indicate groups ranging from the U.S. Chamber of Commerce to the AFL-CIO were able to provide testimony both in support and in opposition to the proposed rule.

## VI. Conclusion

The rulemaking process for the proposed Conflict of Interest rule is ongoing, and the final rule has yet to be published in the *Federal Register*. Because this process is ongoing, the record before the Committee is incomplete and does not reflect the Labor Department or any other agency's final position regarding the rule. As such, broad conclusions about the policy impact or the content of the final rule are premature.

However, a review of the Committee record demonstrates that Labor Department conducted an extensive process to solicit comments and technical assistance from other federal agencies with expertise that may be relevant to the proposed rule. These consultations started after the Labor Department withdrew the 2010 draft rule and continued through the years leading up to the proposal of the revised rule published on April 20, 2015. This process included at least 52 meetings or phone calls with other agencies, including at least eight meetings or phone calls between Secretary of Labor Tom Perez and SEC Chair Mary Jo White.

The Administration also made a significant effort to solicit input from the public and other stakeholders. OIRA held 21 meetings with stakeholders, including industry and consumer advocates, while conducting a formal review of the proposed rule. The Labor Department also held a public comment period on the rule generating 3,134 total comments, including 30 petitions that encompass an additional 386,889 comments. These comments, including those made by Members of Congress and other stakeholders, express a wide range of opinions about the policy impacts of the proposed rule. All of the input submitted during the comment period

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Action, Fixed Insurance Agents, Washington Should Not Limit or Restrict our Advice and Retirement Savings Choices, The Department's Proposed Fiduciary Rule for Retirement Investment Advice is Unworkable, Hard-Working and Concerned Investors, Advance and Alternative to the DOL's Fiduciary Proposal, Writing to Urge the Department of Labor to Reconsider, DOL Limiting Choices in IRAs, Americans for Financial Reform, OTC Securities, and Thank You for Seeking Practical Input on How to Develop a Best Interest Standard.

<sup>26</sup> Testimony was submitted by Center for Retirement Research at Boston College, AARP, James D. Keeney, InvestSense, Financial Planning Coalition, Financial Services Roundtable, Groom Law Group Chartered, Arthur B. Laby, Ron A. Rhoades, Jonathan Reuter, TIAA-CREF, 3ethos, Investment Company Institute (twice), Better Markets (three times), Save Our Retirement, Farmer's Insurance, Russell Investments, Pension Rights Center, America's Health Insurance Plans and Blue Cross Blue Shield Association, American Bankers Association, Raymond James, Association for Advanced Life Underwriting, Benjamin F. Cummings, Center for American Progress, Mercer Bullard, National Active and Retired Federal Employees Association, The Committee for the Fiduciary Standard, Managed Funds Association, American Society of Appraisers, CFA Institute, U.S. Securities Markets Coalition, PIABA (twice), Appraisal Institute, Financial Engines, Indexed Annuity Council, Insured Retirement Institute, and Weyn LLC.

becomes part of the rulemaking record on which the Labor Department must base its reasoning and conclusions.

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OPINIONS  
OF THE  
**OFFICE OF LEGAL COUNSEL**  
OF THE  
UNITED STATES DEPARTMENT OF JUSTICE  
CONSISTING OF SELECTED MEMORANDUM OPINIONS  
ADVISING THE  
**PRESIDENT OF THE UNITED STATES,  
THE ATTORNEY GENERAL**  
AND OTHER EXECUTIVE OFFICERS OF THE FEDERAL GOVERNMENT  
IN RELATION TO  
THEIR OFFICIAL DUTIES

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**FOREWORD**

The Attorney General has directed the Office of Legal Counsel to publish selected opinions on an annual basis for the convenience of the executive, legislative, and judicial branches of the government, and of the professional bar and the general public. The first fourteen volumes of opinions published covered the years 1977 through 1990; the present volume covers 1991. The opinions included in Volume 15 include some that have previously been released to the public, additional opinions as to which the addressee has agreed to publication, and opinions to Department of Justice officials that the Office of Legal Counsel has determined may be released. A substantial number of Office of Legal Counsel opinions issued during 1991 are not included.

The authority of the Office of Legal Counsel to render legal opinions is derived from the authority of the Attorney General. Under the Judiciary Act of 1789 the Attorney General was authorized to render opinions on questions of law when requested by the President and the heads of executive departments. This authority is now codified at 28 U.S.C. §§ 511-513. Pursuant to 28 U.S.C. § 510 the Attorney General has delegated to the Office of Legal Counsel responsibility for preparing the formal opinions of the Attorney General, rendering opinions to the various federal agencies, assisting the Attorney General in the performance of his function as legal adviser to the President, and rendering opinions to the Attorney General and the heads of the various organizational units of the Department of Justice. 28 U.S.C. § 0.25.

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**OPINIONS**  
**OF THE**  
**OFFICE OF LEGAL COUNSEL**

### **Ex Parte Communications During FCC Rulemaking**

Ex parte communications by White House officials to Federal Communications Commission commissioners that advocate positions on the FCC rulemaking proceeding to evaluate financial interest and syndication rules would be permissible.

According to FCC regulations, as interpreted by the FCC General Counsel, communications by the White House must be disclosed in the FCC rulemaking record if they are of substantial significance and clearly intended to affect the ultimate decision.

Although solicitation of the views of White House officials by FCC commissioners would be permissible and need not be included in the rulemaking record, any response by White House officials to such a solicitation would be subject to the same disclosure requirements that apply to unsolicited communications.

January 14, 1991

#### MEMORANDUM OPINION FOR THE DEPUTY COUNSEL TO THE PRESIDENT

This memorandum responds to your request that we answer certain questions regarding ex parte communications between White House officials and Commissioners of the Federal Communications Commission ("FCC") in connection with the FCC's ongoing rulemaking proceeding to evaluate its financial interest and syndication rules relating to television network involvement in the programming marketplace. Specifically, you have asked (1) whether it is permissible for White House officials to contact FCC Commissioners to advocate a position on this rulemaking; (2) whether any such communications would be subject to FCC disclosure requirements; and (3) whether it would be permissible for FCC Commissioners to solicit the views of White House officials and whether any such communications would be subject to the FCC disclosure requirements.

We conclude that the communications by White House officials would be permissible and, according to FCC regulations, they must be disclosed in the FCC rulemaking record if they are of substantial significance and clearly intended to affect the ultimate decision. Solicitations of the views of White

House officials by FCC Commissioners would be permissible and need not be included in the rulemaking record. Any response by White House officials to such a solicitation, however, would be subject to the same disclosure requirements that apply to unsolicited communications.

# I.

We believe it is clearly permissible, as a matter of general administrative law, for White House officials, including senior members from the Council of Economic Advisors and officials from the Office of the Vice President, Office of Management and Budget, and Office of White House Counsel, to contact FCC Commissioners to advocate a position on this rulemaking. This conclusion is compelled by *Sierra Club v. Costle*, 657 F.2d 298 (D.C. Cir. 1981), the leading *ex parte* contacts case under the Administrative Procedure Act ("APA"), 5 U.S.C. §§ 551-559, 701-706.

In *Sierra Club*, an Environmental Protection Agency ("EPA") rulemaking was challenged as procedurally defective in a variety of ways, including that the decisionmaking was influenced by an "undocketed meeting . . . attended by the President, White House staff, other high ranking members of the Executive Branch, as well as EPA officials, and which concerned the issues and options presented by the rulemaking." *Id.* at 404. In holding that the meeting was permissible and need not have been "docketed" (*i.e.*, a summary placed in EPA's rulemaking record),<sup>1</sup> the D.C. Circuit Court of Appeals

recognize[d] the basic need of the President and his White House staff to monitor the consistency of executive agency regulations with Administration policy. He and his White House advisers surely must be briefed fully and frequently about rules in the making, and their contributions to policymaking considered. The executive power under our Constitution, after all, is not shared — it rests exclusively with the President.

*Id.* at 405. The court not only concluded that "[t]he authority of the President to control and supervise executive policymaking is derived from the Constitution," *id.* at 406, but added that

the desirability of such control is demonstrable from the practical realities of administrative rulemaking. Regulations such

<sup>1</sup> The *Sierra Club* holding on "docketing" did not modify the APA case law providing that purely factual and "conduit" (*i.e.*, from interested parties outside the government) information provided in the course of such communications should be included in agency rulemaking records. See *Contacts Between the Office of Management and Budget and Executive Agencies Under Executive Order No. 12,291*, 5 Op. O.L.C. 107 (1981).

as those involved here demand a careful weighing of cost, environmental, and energy considerations. They also have broad implications for national economic policy. Our form of government simply could not function effectively or rationally if key executive policymakers were isolated from each other and from the Chief Executive. Single mission agencies do not always have the answers to complex regulatory problems. An over-worked administrator exposed on a 24-hour basis to a dedicated but zealous staff needs to know the arguments and ideas of policymakers in other agencies as well as in the White House.

*Id.* (footnotes omitted).

Just as the court found in *Sierra Club* that it was permissible under the APA for the President and other White House officials to meet with EPA officials in an effort to influence the results of an EPA rulemaking, we believe it is permissible for White House officials to contact FCC Commissioners in an effort to influence the results of an FCC rulemaking. The constitutional and administrative rationales set forth in *Sierra Club* are fully applicable to the FCC rulemaking on financial interest and syndication rules.<sup>2</sup>

*Sierra Club* makes it clear that, in addition to the general requirements of the APA, any more specific statutory requirements must be considered. *Id.* at 406-07. The only such requirements that we are aware of that might apply in the present situation are those contained in the laws and regulations governing FCC proceedings. The FCC's notice of proposed rulemaking expressly states that the FCC has determined that ex parte communications are permissible in this rulemaking proceeding. See 55 Fed. Reg. 11,222, 11,223 (1990) ("After June 13, 1990, the proceeding will become a non-restricted proceeding, in which ex parte presentations will be permissible, subject to the disclosure requirements set forth in the Commission's rules.") The FCC's ex parte communication regulations, 47 C.F.R. Subpart H, apply by their terms to ex parte communications from any person outside the FCC, expressly including presentations from government officials. See 47 C.F.R. §

<sup>2</sup> *Sierra Club* is not distinguishable on the basis that the FCC, unlike the EPA, might be viewed as an "independent agency." *Sierra Club* is the leading construction of the APA on ex parte contacts during rulemaking, and the APA clearly applies equally to the FCC and the EPA. See 5 U.S.C. § 551(1). Thus, the *Sierra Club* rationale concerning "the practical realities of administrative rulemaking," 657 F.2d at 406, applies fully to all agency rulemaking, whether done by a purely executive or "independent" agency. Indeed, the only exception to its holdings on White House contacts that *Sierra Club* specifically identifies is where the contacts "directly concern the outcome of adjudications or quasi-adjudicatory proceedings," thus implying that all rulemaking is covered by the main holding. *Id.* at 407. Moreover, whatever the constitutionality of restricting the removal of the heads of "independent agencies," there is no doubt that the President has the constitutional authority to inform (directly or through his staff) an "independent agency" of the Administration's program, in an effort to coordinate policy within the executive branch. See *Morrison v. Olson*, 487 U.S. 654 (1988). Accordingly, the President retains authority to attempt to influence rulemaking decisions by "independent agencies" in the ways endorsed in *Sierra Club*.



1.1206(a)(1)-(3) note 1 (“[P]resentations from members of Congress or their staff or from other agencies or branches of the Federal Government or their staff that are of substantial significance and clearly intended to affect the ultimate decision shall be treated as *ex parte* presentations . . .”). Accordingly, we conclude that *ex parte* communications by White House officials in connection with this rulemaking are permissible under the FCC *ex parte* regulations.

Although *ex parte* communications to FCC Commissioners by White House officials are thus legally permissible, we note the current White House policy guidance applicable to contacts with independent regulatory agencies like the FCC. See Memorandum for White House Staff, from C. Boyden Gray, Counsel to the President, *Re: Prohibited Contacts with Agencies*. That guidance states:

As a general rule, no member of the staff should make an *ex parte* contact with a regulatory agency in regard to any particular matter pending before that agency, regardless of whether the proceedings are deemed to be rulemaking or adjudicative, when such a contact may imply preferential treatment or the use of influence on the decision-making process.

. . . White House staff members should avoid even the mere appearance of interest or influence — and the easiest way to do so is to avoid discussing matters pending before the independent regulatory agencies with interested parties and avoid making *ex parte* contacts with agency personnel. Should an occasion arise . . . where it appears necessary [for White House staff] to discuss general policy matters with the staff of an independent regulatory agency, to avoid any appearance of impropriety, [the White House staff individual] should first consult with the Office of the Counsel to the President to determine whether such contact would be appropriate under the circumstances.

*Id.* at 1-2.

## II.

You have also asked whether, if *ex parte* communications to FCC Commissioners by White House officials are permissible, the communications must be publically disclosed: *i.e.*, included in the FCC’s rulemaking record. Although *Sierra Club* makes it clear that such disclosure is not required as a matter of general administrative law, see 657 F.2d at 404-08, the FCC regulations on *ex parte* communications provide for disclosure of certain

communications of that nature. We have consulted the FCC General Counsel's Office to ascertain the FCC's interpretation of its regulations.<sup>3</sup> The following discussion is based on that interpretation.<sup>4</sup>

As noted above, the FCC's notice of proposed rulemaking states that "*ex parte* presentations will be permissible" in this proceeding, "subject to the disclosure requirements set forth in the Commission's rules." 55 Fed. Reg. at 11,223. This statement is consistent with the FCC regulations, which provide that all informal rulemaking proceedings, except proceedings on allotment of specific radio or television channels, are "non-restricted proceedings," *see* 47 C.F.R. § 1.1206(b)(1), in which "*ex parte* presentations are permissible . . . if [certain enumerated] disclosure requirements are met." 47 C.F.R. § 1.1206(a). The regulations specify which communications during a non-restricted proceeding from government sources outside the FCC should be viewed as *ex parte* communications that must be included in the rulemaking record:

Unless otherwise exempted under Section 1.1204, presentations from members of Congress or their staff or from other agencies or branches of the Federal Government or their staff that are of substantial significance and clearly intended to affect the ultimate decision shall be treated as *ex parte* presentations and placed (if oral, a written summary of the presentation shall be prepared and placed) in the record of the proceeding by Commission staff or in accordance with the procedures set forth in Section 1.1206(a)(1)-(3).

47 C.F.R. § 1.1206(a)(1)-(3) note 1. Thus, unless otherwise exempted under section 1.1204(b), all *ex parte* communications from government officials or employees that "are of substantial significance and clearly intended to affect the ultimate decision" must be placed in the rulemaking record. If the communications are oral, they may be placed in the record either by the means of a written summary prepared by Commission staff or by a written memorandum submitted by the *ex parte* "communicator" on the day of the communication. 47 C.F.R. § 1.1206(a).

Accordingly, the FCC regulations require the placement in the FCC rulemaking record of a memorandum summarizing any *ex parte* communication by a White House official to an FCC Commissioner in which the White House official advocates a position on this rulemaking, so long as the communication is "of substantial significance and clearly intended to affect the

<sup>3</sup> We consulted David H. Solomon, Assistant General Counsel, Administrative Law Division.

<sup>4</sup> We do not address in this memorandum the authority of the President to direct the FCC to change its regulations.

ultimate decision.” The regulations apply by their terms to all parts of the government and make no exception for communications from White House officials. Nor would any of the section 1.1204(b) exemptions appear to be applicable. In particular, the FCC does not believe that exemption (5) is available. See 47 C.F.R. § 1.1204(b)(5) (exempting presentations “to or from an agency or branch of the Federal Government or its staff [that] involve[] a matter over which that agency or branch and the Commission share jurisdiction”). In the view of the FCC General Counsel’s Office, the exemption for agencies that “share jurisdiction” pertains only to other federal agencies that exercise statutory authority that overlaps with the FCC’s authority; it is not addressed to a government entity that might supervise the FCC. Accordingly, the White House does not, within the meaning of the exemption, “share jurisdiction” with the FCC over financial interest and syndication rules. We believe that the FCC’s interpretation of exemption (5) is reasonable.

### III.

Finally, you have asked whether it would be permissible for an FCC Commissioner to solicit the views of White House officials and whether any such solicitation would be subject to the FCC disclosure requirements. We are unaware of any statutory or regulatory provisions that would prohibit such a solicitation or require that it be included in the rulemaking record. The conclusions reached above regarding *Sierra Club* should apply equally to a solicitation by an FCC Commissioner, because nothing in the court’s rationale suggested that the protection of ex parte White House communications should be “one-way”: i.e., protecting communications by White House officials but not to them.

Moreover, nothing in the FCC regulations would preclude such a solicitation (indeed, the regulations contemplate solicitations, see 47 C.F.R. § 1.1206(a)(3)) or require that it be docketed. The FCC General Counsel’s Office has advised us that solicitations are permissible and whether they are recorded in the rulemaking record is discretionary. Any communication by a White House official in response to a solicitation, however, would be subject to disclosure under the same standards governing unsolicited communications. See 47 C.F.R. §§ 1.1204(b) note, 1.1206(a)(3), 1.1206(a)(1)-(3) note 1.

### CONCLUSION

Ex parte communications by White House officials to FCC Commissioners that advocate positions on the ongoing FCC rulemaking proceeding to evaluate financial interest and syndication rules would be permissible. According to FCC regulations, as interpreted by the FCC General Counsel’s Office, such communications must be disclosed in the FCC rulemaking record

if they are of substantial significance and clearly intended to affect the ultimate decision. Solicitations of the views of White House officials by FCC Commissioners would be permissible and need not be included in the rulemaking record. Any response by White House officials to such a solicitation, however, would be subject to the same disclosure requirements that apply to unsolicited communications.

JOHN O. MCGINNIS  
*Deputy Assistant Attorney General*  
*Office of Legal Counsel*

**Post-Hearing Questions for the Record  
Submitted to the Honorable Bradford P. Campbell  
From Senator Rob Portman**

**Homeland Security and Governmental Affairs Hearing: “The Administrative State: An  
Examination of Federal Rulemaking”  
April 20, 2016**

1. Mr. Campbell, you’ve warned in the past year that the fiduciary rule will make it more difficult for small businesses to set up a retirement plan and obtain investment advice for their employees. Experts have further maintained that the “seller’s exemption”, which prohibits brokers from selling retirement plans to small businesses, is even more poorly designed under the final rule it was than under the proposed rule. For example, under the final rule, it is illegal to sell to a small business with assets less than \$50 million, regardless of the business’ number of employees.

Are estimations available yet regarding how many small businesses in your estimation will lose access to their retirement plan under the final rule? Additionally, how many small businesses will lose access to a retirement plan going forward due to reduced services available to them under the rule?

2. One change in the final rule that has received a lot of attention is the DOL’s extension of the rule’s implementation period from eight months to one year, with the rule taking full effect in January 2018. In your estimation, does this newly extended timeline constitute a significant change with respect to overall breadth of retirement services the financial services industry will ultimately be able to offer?

**Witness responses to questions submitted for the record were not received  
by time of printing.**

**Post-Hearing Questions for the Record  
Submitted to the Honorable Bradford P. Campbell  
From Senator Jon Tester**

**Homeland Security and Governmental Affairs Hearing: “The Administrative State: An  
Examination of Federal Rulemaking”  
April 20, 2016**

Mr. Campbell, I’ve been fairly skeptical about the Department of Labor’s Fiduciary rule for quite some time now. I had concerns with the original proposal in 2011 and I had concerns with the re-proposal last year. Now it appears that the Department has addressed a number of concerns that I raised, but I’m still not quite convinced this rule won’t cut off access to advice and products that are critically important to middle-class Americans looking to save for retirement.

- 1) Would you please share with the Committee your thoughts on the final rule.
- 2) Do you believe this rule will limit access to advice and products that currently exist?

**Witness responses to questions submitted for the record were not received  
by time of printing.**